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List of abbreviations

A.C.	Appeal Cases
A.C.L.R.	Australian Company Law Reports
AcP	Archiv für die civilistische Praxis
All ER	All England Law Reports
BAG	Bundesarbeitsgericht
BB	Der Betriebsberater
BGH	Bundesgerichtshof
Ch. D.	Chancery Division
CLJ	Cambridge Law Journal
Columbia L. Rev.	Columbia Law Review
Con. L.R.	Construction Law Reports
D.L.R.	Dominion Law Reports
Ed.	editor
F.	Federal Reporter
F. Supp.	Federal Supplement
JuS	Juristische Schulung
JZ	Juristenzeitung
LQR	The Law Quarterly Review
LM	Lindemaier-Möhring (Nachschlagwerk)
L.T.	Law Times
MDR	Monatsschrift des Deutschen Rechts
MLR	Modern Law Review
n.	footnote
NJW	Neue Juristische Wochenschrift
NJW-RR	Neue Juristische Wochenschrift – Rechtsprechungsreport
NSWLR	New South Wales Law Reports
NZLR	New Zealand Law Reports
OJLS	Oxford Journal of Legal Studies

Q.B.	Queen's Bench
RGZ	Entscheidungen des Reichsgerichts in Zivilsachen
RIDC	Revue Internationale de Droit Compare
SA	South African Law Reports
SALJ	South African Law Journal
T.L.R.	Times Law Reports
Tul. L. R.	Tulane Law Review
U.S.	United States Supreme Court
V.R.	Victorian Reports
W.L.R.	Weekly Law Reports
WM	Wertpapiermitteilungen
ZeuP	Zeitschrift für Europäisches Privatrecht

A. Introduction

There are a number of circumstances in which parties, that enter into negotiations to conclude a contract, incur losses because the anticipated contract does not materialise. The parties could for example think that they concluded a contract, which is, however, void or an offeror sends together with his offer goods to a long known customer, wrongfully trusting that a contract will come about. Furthermore, the parties could have entered into lengthy negotiations about a costly project which do for some reason not ripen into a contractual agreement. In all these situations the parties might have made expenses with regard to the prospective contract that are now lost without any reward in return.

The present thesis deals only with cases where negotiations failed, before a contract ever came about and where the aggrieved party suffered purely economic losses.[1]

Over the last decades more and more cases came to the courts where a party claimed costs or lost profits, that it incurred because a promising deal went off in the precontractual phase.[2] The traditional view emphasises the principle of the 'freedom of contract' which entails the negative freedom of contract, i.e. the privilege not to enter into a binding agreement.[3] It was concluded that each party must be free to walk away from the deal without the risk of precontractual liability.[4] A party that enters negotiations in the hope of the gain that will result from ultimate agreement bears the risk of whatever loss results if the other party breaks off the negotiations.[5] The expenses are

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[1] There are cases where one party disregards the due confidentiality during negotiations and, thus, violates a property right such as a marketing idea or a trade secret, see: *E.I. Du Pont de Nemours Powder Co.* v. *Masland*, 244 U.S. 100, 102 (1917).

[2] English cases: *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409; *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) 1 Q.B. 428; *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 1 WLR 932 (Q.B.); *Regalian Properties plc v. London Dockland Development Corp.* (1995) 1 All ER, 1005; American cases: *Reprosystem, B.V.* v. *SCM Corp.* 727 F 2d 257 (2d. Cir.); *Burst* v. *Adolph Coors Co.*, 503 F. Supp. 19, 23 (E.D. Mo. 1980).

[3] Freedom *from* contract as opposed to the positive freedom of contract which is the freedom *to* contract, Nili Cohen, *Pre-Contractual Duties: Two Freedoms and the Contract to Negotiate*, in: D. Friedmann & J. Beatson (eds.), *Good Faith and Fault in Contract Law* (1995), at 25, 27 and 34.

[4] *Schreiber* v. *Dinkel* (1886) 54 L.T. 911, at 912 is the earliest case that enunciated the principle that a party spending money or labour precontractually cannot expect to be rewarded for its expenses, since the other party is free to walk away from the deal. Also: E.A. Farnsworth, Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations, *Columbia L. Rev.* 87 (1987), at 221; in Germany: Art. 2 (2) GG, K. Larenz, *Allgemeiner Teil des Deutschen Bürgerlichen Rechts*, (1980), at 473; in Israeli law, Art. 3 (a) Law of contracts, A. M. Rabello, La Theorie de la "Culpa in Contrahendo" et la loi israelienne sur les contrats 1973, vol. 49 *RIDC* (1997), at 59 ,60.

[5] *Schreiber* v. *Dinkel* (1886) 54 L.T. 911 and 912.

regarded as those of his business which he hopes will be met out of the profits of contracts that are successfully made.[6] Accordingly, courts didn't grant precontractual liability per se.

During the second half of this century, however, it has been acknowledged that a party needs protection, if it reasonably trusted that a contract would come about, and therefore, incurred expenses which turned out to be futile as the other party unjustifiably ended the negotiations. Some courts and authors don't believe that the freedom of contract is going so far as to allow a party to unjustifiably break off negotiations and leaving the other party with horrendous expenses for which there is no recovery.

A number of remedies have been invoked to overcome the harsh denial of recovery: The Anglo-American legal systems in particular accepted claims that were grounded on unjust enrichment[7]; a South African case dealt with precontractual liability as a matter of misrepresentation[8] and in civilian jurisdictions such cases fall under a specific quasi-contractual claim, the *culpa in contrahendo*[9].

All these legal foundations grapple with the problems that are inherent in precontractual claims. For example with the question which requirements should be employed to reasonably limit the possibility of recovery. The law doesn't want to interfere too severely with negotiations in view of the - still validly considered - freedom of contract. Is it, therefore, necessary that the defendant acted with fault? And can it be regarded as 'fault' to break off negotiations when each party is in principle free to do so? Another difficult issue is which costs can be recovered. The plaintiff will mostly be granted reliance, but not expectation losses.[10] Hence, he can claim the expenses that he made with regard to the prospective contract but not the profits that he expected to get as a result of an agreement. Whether he can recover the profits of opportunities that the plaintiff let go because of the negotiations is also an unanswered question. These lost profits could theoretically be part of the reliance loss but it could also be considered as going too far to concede those, because it seems to be exactly the risk a partner takes when he enters into exclusive negotiations.

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[6] *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 1 WLR 932, at 934 Q.B.

[7] E.A. Farnsworth, *supra* n. 4, at 222, 229 - 233; Goff & Jones, *The Law of Restitution*, (1993), at 554 ff.

[8] *Murray* v. *McLean, N.O.*, (1970) 1 SA 133; misrepresentation is also employed in the United States as basis of liability, E.A. Farnsworth, *supra* n. 4, at 233 - 236.

[9] Emmerich, in: K. Rebmann / F-J. Säcker (eds.), *Münchener Kommentar zum Bürgerlichen Gesetzbuch*, Band 2 (1994) (in the following: MüKo), Vor § 275, digit 158 ff; RGZ 151, 357; BGH NJW 1975, 1774.

[10] One couldn't possibly force the other party to enter into the contract, E.A. Farnsworth, *supra* n. 4, at 223.

The following chapters will try to illuminate how different legal systems handled these problems of precontractual liability. Maybe some suggestions come up with regard to the legal foundations and the extent of liability.

B. Restitution

Restitution has been taken as a basis for the liability of a party that breaks off negotiations in England and also in Australia.

The law of restitution is the law relating to all claims, quasi-contractual or otherwise, which are founded upon the principle of unjust enrichment. In these cases the defendant has received something - money, other goods or services, i.e. any benefit - without a legal *causa,* whereas the plaintiff is entitled to have that money or good or to receive payment for his services. Then the defendant is obliged in justice to restore this benefit to the plaintiff.[11]

In English law the principle of restitution for unjust enrichment has long not been accepted as part of the law. Still today adjudication has not formulated a general rule giving a plaintiff the right of recovery of the unjust enrichment from the defendant, [12] although, some recent decisions seem to have at last established unjust enrichment as an independent ground of relief.[13] Hence, the reasoning to reverse the unjust shift of a benefit is the basis of restitutionary claims. Restitution will be appropriate to deal with precontractual liability if the abortion of negotiations leads to an unjust shift of a benefit from the plaintiff to the defendant. In order to analyse whether this is the case, we need to look at the requirements of a claim under restitution.

I. Difficulties of restitution in general

Very simplified a restitutionary claim presupposes three things: First, the defendant must have been enriched by the receipt of a benefit. Secondly, that benefit must have been gained at the

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[11] Goff & Jones, *supra* n. 7, at 3, 12; A.S. Burrows, Contract, Tort and Restitution - A Satisfactory Division or not?, *LQR* 99 (1983), at 232.

[12] *Re Cleadon Trust* (1938) 4 All ER 518, at 530; and even in a relatively young case Lord Diplock denied the existence of a general doctrine of unjust enrichment: *Orakpo* v. *Manson Investment Ltd.* (1978) A.C. 95, 104, A. S. Burrows, *supra* n. 11, at 233.

[13] *Lipkin Gorman* v. *Karpnale Ltd.* (1991) A.C. 548, at 558, 559, 568, 577 - 578; *Woolwich Equitable Building Society* v. *Inland Revenue Commissioners* (1992) 3 WLR 366, at 374, 384 - 5, 394, 403 - 4, 414 - 6, 421; E Schrage & B Nicholas, *Unjust Enrichment and the Law of Restitution: A Comparison*, in: E Schrage (ed.), *Unjust Enrichment, The Comparative Legal History of the Law of Restitution*, at 10; R Cook, Reviews and Notices, *LQR* 108 (1992), at 334; F D Rose, General Average as Restitution, *LQR* 113 (1997), 569; B. Dickson, Unjust Enrichment Claims: A Comparative Overview, *CLJ* 54 (1995) 100, at 105.

plaintiff's expense. Thirdly, it would be unjust to allow the defendant to retain that benefit.[14] All of these requirements are complex in themselves and are closely interrelated. Therefore, they cannot be schematically applied to cases of failed negotiations. For the purpose of comprehensibility it is better to point out, beforehand, the problems that restitution faces in general. Then, we will look at the here relevant case law, and finally, see how well the law of restitution applies to situations where the plaintiff claims recovery of precontractual expenses.

1. Benefit

To have a viable action in restitution it is not sufficient or even necessary that the plaintiff suffered a loss. He must show that the defendant received a benefit.[15] This benefit is crucial in restitutionary claims, because it determines what the plaintiff is entitled to recover. Furthermore, it can be an early limitation of restitutionary claims, according to the more or less broad conception of 'benefit' that the law adopts. The problem to define and limit the notion of a 'benefit' is not confined to cases of precontractual liability but haunts the whole law of restitution.

Benefits can be categorised as follows: They can be negative or positive. A positive benefit exists where the defendant receives something tangible that can be realised in money - i.e. money, chattels or an improvement of land. A benefit is negative, when the defendant saved an expense that he could otherwise have incurred - i.e. in the case of the receipt of services or the use of another's chattel. Such positive or negative benefits can be valued objectively or subjectively: The benefit is objective, where every reasonable person would consider the defendant enriched and it is subjective, where the defendant himself assigns a different, higher or lower value to the - positive or negative - benefit that he received.[16]

The direct payment of money to the defendant is objectively and positively benefiting the defendant, so that these cases don't present a problem.[17]

It becomes more complicated when the plaintiff rendered services or incurred expenditure in the interest of the defendant, because of the recognised value of the defendant's freedom of choice,

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[14] Goff & Jones, *supra* n. 7, at 16; B. Dickson, *supra* n. 13, at 106.

[15] M. McInnes, Restitutionary Relief for Incontrovertible Benefits, *LQR* 109 (1993), 521, at 524.

[16] A Burrows, *The Law of Restitution* (1992), at 8.

[17] Goff & Jones, *supra* n. 7, at 17 - 8; P. Birks, *An Introduction to the Law of Restitution*, Oxford 1985, at 109; M. McInnes, *The Structure and Challenges of Unjust Enrichment*, in: M. McInnes (ed.), *Restitution: Developments in Unjust Enrichment*, at 21; A. Burrows, *supra* n. 16, at 10.

namely the choice what to spend his money on.[18] From their very nature services cannot be restored and the defendant may never have wished to receive them or to receive them if he had to pay for them.[19] However, since the old case of *Planche* v. *Colburn* it has been acknowledged that the rendering of services can in principle constitute a legal as well as an economic benefit in that the defendant saves the cost of the received services – i.e. he has a negative benefit.[20] Nevertheless, there is dispute about the limits of such a broader notion of 'benefit'.

We will see that in most of the situations where negotiations fail the plaintiff rendered services or incurred expenses in the interest of the future contract, e.g. by making plans or estimates or by preparing his production. In any case, the defendant will often not have received anything tangible at that stage. Hence, the difficulties in determining when there is a recognisable negative benefit arises fully in our cases.

a) The dilemma

The discussion evolves around the so-called 'subjective devaluation'. People do not invariably agree on what constitutes an enrichment. Though, a certain service may generally be considered enriching and may have an objective market value, the defendant may subjectively not consider himself to be enriched.[21] The difficulty consists in finding a balance between the two extreme positions. On the one hand one could accept any subjective devaluation. Then the defendant would be able to invoke every subjective reason he has to deny that he was enriched, however unreasonable it might be. On the other hand one could allow the defendant to deny enrichment

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[18] M. McInnes, in M. McInnes (ed.), *supra* n. 17, at 20.

[19] Goff & Jones, *supra* n. 7, at 18.

[20] (1831) 8 Bing 14. This decision is frequently criticised because the defendant didn't receive anything, hence, there was no corporeal objective benefit; A. Burrows, *supra* n. 16, at 8 - 9; M Garner, The Role of Subjective Benefit in the Law of Unjust Enrichment, *OJLS* 10 (1990), 42, at 53 - 54.
For further adjudication: *Re Wyvern Developments Ltd.* (1974) 1 W.L.R. 1097, 1105; It was thought, though, at a time, that the plaintiff has to demonstrate that the defendant gained a positive, as distinct from a negative benefit, Goff & Jones, *supra* n. 7, at 17; *Phillips* v. *Homfray* (1883) 24 Ch. D. 439, 454 - 455; *Government of India* v. *Taylor* (1955) A.C. 491, 513; *Strand Electric and Engineering Co.* v. *Brisford Entertainment Ltd.* (1952) 2 Q.B. 246, at 252, 253 - 55; A Burrows, *supra* n. 16, at 8, Goff & Jones, *supra* n. 7, at 17; J. Mannolini, Restitution where an Anticipated Contract Fails to Materialise, *MLR* 59 (1996), 111, at 112, P Key, Detrimental Reliance in Anticipation of a Contract, *LQR* 111 (1995), 576, at 577.

[21] The example of shoeshine illustrates the dilemma quite well: although the polishing of shoes usually has a certain market value, the defendant that gets his shoes polished may prefer to have his shoes dirty or may be indifferent as to how his shoes look like and doesn't want to spend money on it. M McInnes, in: McInnes (ed.), *supra* n. 17, at 20.

only if it objectively doesn't benefit the defendant, i.e. each time that a service rendered has an objective market value, the defendant would not be entitled to deny that he is enriched.
A lot of attempts have been made to find a reasonable way of defining when works done in the interest of the defendant can be regarded as a 'benefit' or 'enrichment' in the law of restitution.

b) Possible solutions

Generally scholars agree that the requirement of enrichment should be satisfied when the defendant receives a so-called 'incontrovertible' benefit, i.e. one which no reasonable person can deny.[22] This category covers the cases where already the objective appearance of an enrichment predominates to such a degree that they must obviously be included in restitution.
There is a further group of cases where academics refuse the defendant to argue that he has not received a benefit because of his subjective evaluation of the services conferred. That is, when the defendant - through his conduct - made the plaintiff believe that he wants to receive, and hence, would pay for the services. Because of the inevitable difficulty to determine, when the defendant showed such sufficiently 'enticing' conduct, there is dispute about the 'principle' that best limits the recognisable benefit of the defendant while respecting his freedom of choice.

(1) Incontrovertible benefit

There is no consensus as to how an 'incontrovertible' benefit is identified.[23] The prime example of an incontrovertible benefit is when a reasonable person would conclude that the plaintiff saved the defendant an expense which he otherwise would necessarily have incurred, for example when a service was indispensable to sustain the defendant's house.[24] If the expense is necessary the defendant cannot take recourse to 'subjective devaluation', since he doesn't have a choice if he wants to spend his money for this expense or not.[25]
Another group of incontrovertible benefits is the one of realised or realisable gains. The supposition is that a person cannot reasonably deny to have been enriched if he realised a financial

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[22] P. Birks, *supra* n. 17, at 116 - 124; Goff & Jones, *supra* n. 7, at 22 - 26; A. Burrows, *supra* n. 16, at 9 - 11; M. McInnes, *supra* n. 15, at 523.
[23] M. McInnes, in: M. McInnes (ed.), *supra* n. 17, at 21.
[24] Goff & Jones, *supra* n. 7, at 23; A. Burrows, *supra* n. 16, at 10 - 11.
[25] M. Garner, *supra* n. 20, at 42 - 4. In this category the difficulty consists to determine in which cases an expense is truly 'necessary'. It surely is if there is a legal obligation of the defendant to pay, and also, if there is a factual obligation to pay (e.g. in order to sustain a house).

gain from the services conferred by the plaintiff,[26] for example by selling the improved car for a higher price. In that case the defendant is as well off as if the plaintiff would have given him cash money.[27] Again, the defendant cannot 'subjectively devalue' the benefit, because there is a positive and objective accretion to his wealth.[28]

(2) Free acceptance vs. Request vs. 'Bargained-for' Benefit

Where the defendant displayed a certain conduct, which makes a reasonable plaintiff believe that he will pay for the received services, several 'principles' compete to distinguish deserving cases from undeserving cases of an enrichment. These are the 'principle of free acceptance' of a service, the idea that the defendant 'requested' a service and lastly, the surmise that the defendant 'bargained for' the benefit that he then received.

The 'principle of free acceptance' was formulated by Goff and Jones. They consider that a defendant 'will be held to have benefited from the services rendered if he, as a reasonable man, should have known that the plaintiff who rendered the services expected to be paid for them, and yet he did not take a reasonable opportunity open to him to reject the proffered services'.[29] Because his conduct shows that he values what was offered to him, he cannot resort to 'subjective devaluation' under which he would have to argue that he did not value the services.[30] Under this definition also a bystander, who is indifferent as to whether, for example, his windows are cleaned or not, would be regarded as having benefited. If he wouldn't have wanted them cleaned, he could have said so, and since he didn't object a reasonable person will trust that he is going to pay for

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[26] P. Birks, *supra* n. 17, at 121; M. McInnes, *supra* n. 17, at 22.

[27] M. Garner, *supra* n. 20, at 44; M. McInnes, *supra* n. 17, at 22.

[28] M. Garner, *supra* n. 20, at 44. Authors disagree as to whether the gain has to be already **realised** – i.e. already converted into cash -: P. Birks, *supra* n. 17, at 121 – 124, compare the case of *Greenwood* v. *Bennett* (1973) Q.B. 195, at 197. Or whether the gain must only be **easily realisable** – i.e. when the defendant can realise the 'cash value' of the service without hindrances, regardless of whether he converts it into cash or not: Goff & Jones, *supra* n. 7, at 23. Or whether it must be a **readily realisable** gain – which is the case if it is reasonably certain that the defendant is soon going to realise a financial gain from the conferred service: A Burrows, *supra* n. 16, at 10 – 11. Although these formulas never entered into the case law, some decisions can well be explained on the basis of these considerations: *Greenwood* v. *Bennett* (1973) 1 Q.B. 195, 202; *William Lacey (Hounslow)* v. *Davis*, (1957) 2 All ER 712.

[29] Goff & Jones, *supra* n. 7, at 18 - 22, also P. Birks, *supra* n. 17, at 109 - 17, compare the cases: *Brenner* v. *First Artists' Management Pty Ltd* (1993) 2 V.R. 221, at 257 and 260, where Byrne J. expressly employed this test.

[30] P. Birks, *supra* n. 17, at 114 - 5, after criticism from other scholars for the principle's failure to protect adequately the defendant's freedom of choice, especially P. Birks supported the theory. He clarified that the 'free acceptance' rules doesn't intend to establish subject enrichment, but precludes the subjective devaluation of an objective benefit because of the 'reproachable' conduct of the defendant. See P Birks, *In Defence of Free Acceptance*, in Burrows (ed.) *Essays on the Law of Restitution* (1991) 105, at 129.

the cleaning. Evidently, the burden of 'action' to prevent the plaintiff from squandering his resources on the service is lying on the defendant.

Another view says that this principle of free acceptance goes too far. Only if the defendant 'requested' the services, he can be held liable. Otherwise his freedom of choice is eroded, as he is compelled to pay for a service which he didn't chose to receive.[31] The notion of a 'request' suggests that the defendant must have expressly asked for the services. Sometimes, however, it might be too strict to expect an express request, for example if the defendant encouraged the plaintiff to render the services but didn't 'request' them as such.[32]

Quite similar and also opposing the more liberal 'principle of free acceptance', but not demanding an express request is the 'bargained-for' benefit. This test is not satisfied by mere acquiescence to the rendering of the services. It requires that the defendant indicates, by means of a positive act of bargaining, that he wishes to receive the benefit.[33] The outward appearance of such behaviour suggests a willingness to pay, and therefore, precludes recourse to subjective devaluation. Similar, but a little stricter is Garner's suggestion to see an enrichment only if the plaintiff establishes that the defendant wanted to receive the benefit in question *and* was willing to pay for it as a present priority.[34] This last requirement is not adding too much to the previous ones. In each of the tests it is deducted from the defendant's conduct, that he values the service and, accordingly, a reasonable person can expect him to pay for it. If the defendant doesn't want to pay for the services he must either have shown this through his conduct. Or if he didn't direct his conduct in this regard, he should bear the burden of his ambiguity and a reasonable plaintiff who relied on him, should not suffer from such a defendant's caprice.

c) Conclusion

This outline shows how difficult it can be to argue successfully that the defendant was enriched. We will have to find out later which category and which test is most apt to distinguish when the plaintiff can justifiably claim to recover his precontractual expenses as a 'benefit' from the defendant by applying these tests to cases of failed negotiations.

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[31] P Matthews, Freedom, Unrequested Improvements, and Lord Denning, *CLR* 40 (1981), 340, at 355 - 7.

[32] This was the case in *Regalian Properties plc.* v. *London Docklands Development Corp.* (1995) 1 All ER 1005, at 1008; P Key, *supra* n. 20, at 579.

[33] A Burrows, *supra* n. 16, at 14 - 5.

[34] M Garner, *supra* n. 20, at 51 - 2

2. At the plaintiff's expense

The second element of the concept of unjust enrichment demands that the defendant's enrichment was gained 'at the plaintiff's expense'.

Typically, this is established, when wealth was subtracted from the plaintiff and passes to the defendant, this is the so-called 'subtractive enrichment'.[35] Alternatively, the defendant's gain may be at the plaintiff's expense when he received it as a result of committing a wrong against him, this is the 'enrichment by wrongs'. Such wrongs are defined on the basis of private law notions of culpable conduct.[36]

When negotiations fail the plaintiff will often claim restitution for working time or expenses that he dispensed and that was, accordingly, subtracted from his resources. It seems that this requirement will not present many problems for a claim under precontractual liability.

3. Unjust factor

Lastly, to ground a claim on restitution, the enrichment that the defendant incurred on the plaintiff's expense must have been 'unjust'. This 'injustice' does not denote simple and subjective perceptions of fairness and justice, but rather a variety of distinct categories of cases, where the law recognises that the defendant has to make just restitution for his benefit to the plaintiff.[37]

Since English law only recently recognised a principle of unjust enrichment, there is no case law that established categories of unjust cases. The academics that are concerned about the law of restitution ascertained several categories, but disagree about which groupings should be made.[38]

There is also dissension with regard to the cases of contracts that do not materialise.

Some authors regard them as cases of 'free acceptance', which is likewise considered as an unjust factor and not merely as a factor to determine the defendant's benefit. Others denote them as cases

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[35] M. McInnes, in: M. McInnes, *supra* n. 17, at 30; A. Burrows, *supra* n. 16, at 16.

[36] M. McInnes, in: M. McInnes, *supra* n. 17, at 31 and 37, hence, the plaintiff must establish a private law cause of action. This category in restitution is based on the moral principle that 'no man shall profit from his own wrong', A. Burrows, *supra* n. 16, at 18. Burrows, however, opposes the idea of regarding the restitution for wrongs as an own category of the plaintiff's expenses, see Burrows, *supra* n. 16, at 17 - 20, where he argues that the correlation between the loss of the plaintiff and the gain of the defendant is a strict one. It cannot be overcome by restitution for wrongs, where the plaintiff must not establish, that he lost the equivalent amount than what the defendant gained, but only that a wrong was committed.

[37] *Pavey and Matthews Pty Ltd.* v. *Paul* (1987) 162 CLR 221 at 256 - 7; *Lipkin Gorman* v. *Karpnale Ltd. (H.L. (E.))*, (1991) 2 A.C. 548, at 578; A. Burrows, *supra* n. 16, at 21.

[38] A. Burrows, *supra* n. 16, at 21 - 2.

of '(total) failure of consideration', often because they don't recognise the principle of free acceptance.[39]

At this stage of our analysis of precontractual liability it is merely necessary to explain these two tests which are the only suitable ones when negotiations are arbitrarily broken off.

a) Failure of consideration

The argument for the application of the 'failure of consideration' goes as follows: Failure of consideration means that there has been a failure of what the plaintiff was promised in return for rendering the benefit to the defendant.[40] This stems from the meaning of consideration in contract law. There, consideration is the element that is necessary to make binding every contract, it is the compensation, the counter-performance, for something promised or done.[41] The failure of consideration constitutes an unjust factor because the basis for the plaintiff's conferral of the benefit has been undermined.[42]

In precontractual dealings there is no contractual promise that can fail, but the defendant's conduct during negotiations can conceivably generate the plaintiff's trust that his efforts for the anticipated contract will be rewarded. When the deal then goes off his motivation for rendering precontractual services is disappointed.

b) Free acceptance

The principle of free acceptance has the ambiguous character of establishing that the defendant has been benefited and also that his enrichment is unjust.

The principle states, that the recipient defendant is enriched when he knows that a benefit is being offered to him non-gratuitously and, having the opportunity to reject, he elects to accept it.[43] The enrichment is regarded as unjust, because it is regarded as unconscientious of the recipient to not

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[39] A. Burrows, *supra* n. 16, at 29

[40] A. Burrows, *supra* n. 16, at 251.

[41] H. Ivamy, *Mozley & Whiteley's Law Dictionary,* (11.ed.) 1993, at 57.

[42] *Fibrosa Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.* (1943) A.C. 32, at 48. There is discussion about whether the failure must be complete or merely partial. The traditional requirement demands that the failure is total. But new voices say that there must also be restitution, if the consideration fails only partly, A. Burrows, *supra* n. 16, at 253, 259 - 61.

[43] P. Birks, *supra* n. 17, at 265.

avail himself of the opportunity to save the intervening plaintiff from the risk of rendering his services unpaid.[44]

During negotiations the two parties are in close contact so that the defendant will mostly have a chance to clarify his position and restrain the plaintiff from incurring expenses when he considers the anticipated contact as too uncertain. Then, one can regard him as having 'freely accepted' the works.

4. Conclusion

At first sight the requirements for a restitutionary claim can be applied to cases of precontractual liability for abandoned negotiations, although, the law of restitution is obviously not tailor-made for these cases, and might bring about painful difficulties to argue a claim.

II. Review of the relevant case law

Since restitution is a new concept there is not much case law on restitution for broken off negotiations.[45] Nevertheless, there are several precedents for the recovery of money expensed or services rendered in aspiration of a contract which were brought under disparate actions. These cases unveil – although incoherently, but in substance – the criteria that judges looked at to give or to deny a claim. Therefore, a chronological survey of the most important cases will help to scrutinise the merit of the law of restitution in dealing with precontractual liability.

1. *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.*[46]

In this case the plaintiffs wanted to let some premises to the defendants. Before the contract of lease was concluded, the plaintiffs agreed to alter the premises for the defendants into offices. The defendants agreed to pay the costs of the alterations. The plaintiffs were, however, not owner of the said premises, but only their lessees.

The plaintiffs completed the alterations at the premises, but the lease couldn't be concluded, because the owner of the property didn't give his consent for the sublease to the defendants. The plaintiffs then claimed to costs for the alterations which the defendants had formerly agreed to pay. The court rejected the claim.

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[44] P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 111.

[45] Merely the case of *Regalian Properties plc* v. *London Dockland Development Corp.* (1995) 1 All ER 1005 in English law and *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880 in Australian law.

[46] (1952) 2 T.L.R. 409.

The court asked the crucial question, where the loss should fall after the whole transaction had failed. The plaintiffs had to bear the costs of alterations. The decisive factors were for one that the **benefit** of the alterations would fall with the plaintiffs as they were in possession of the premises. The defendants, however, would have had to pay for the alterations without getting anything in return. Secondly, the **reason for the failure of the lease lay in the sphere of the plaintiffs**. They held themselves out as in a position to grant the sublease and knew or must have known about the requirements they had to meet to be able to grant a sublease. Therefore, when they spent money on the alterations before having secured with their lessors if the sublease will be granted, they were considered to have taken the risk of having to pay for them. Because they took the risk and the defendant couldn't know anything about further requirements they had to pay for the alterations.[47] The two criteria that have to be kept in mind are, first, the benefit - which was here the improvement of leased premises and stayed with the plaintiff -, and, secondly, the fact that the reason for the failure stemmed from the sphere of the plaintiff.

2. *Brewer Street Investment Ltd.* v. *Barclays Woollen Co. Ltd.*[48]

In this case the parties also negotiated about a prospective lease. The parties made the negotiations 'subject to contract', which means that their partly agreements should only be binding when finally a contract would be concluded. The plaintiffs were the owners of the premises and after the negotiations had proceeded so far that both parties were confident that a lease would be entered into, they accepted to make certain alterations. The defendants, who were the future tenants, had requested those alterations for their purposes and undertook the responsibility to pay for them.

Finally the matter went off, because the parties were unable to agree on a term of the lease concerning a possible future sale of the premises to the defendants. The work on the alterations was stopped and the plaintiffs sued the defendants for the amount they had paid to their contractor as 'money paid to the use of the defendants at the defendants' request in respect of the cost of alterations'. The court granted the action.

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[47] (1952) 2 T.L.R. 409, at 413.
[48] (1954) 1 Q. B. 428.

a) Reasoning of the judgement

First the court stated that there was a contract with regard to the alterations and that this contract was an independent contract which was not - as the defendants had submitted -subject to the lease being entered into.[49] They were deemed to be responsible for the costs of alterations, because these were only done upon their **request**, and furthermore, if they **decided entirely on their motion not to go on** with the lease they must also bear the risk of costs.[50] Additionally, the court stressed the fact that the plaintiffs were at all times willing and able to enter into the contract of lease.[51]

The majority decision didn't base the claim on restitution but held the defendants bound by their agreement to pay.

It was Denning L.J., who remarked that the claim could only be based on restitution, since in truth the agreement to pay for the alterations had not become binding.[52]

He compared this case with the case of *Jennings & Chapman* and concluded that in both cases the parties made expenses upon a fundamental assumption - that the lease would be granted - which turned out to be wrong. He also asked where the loss should fall in such circumstances and concluded that the defendants had to pay for the alterations. He didn't regard any party as being at fault, as they fell out on a point which had never been agreed upon. As everyone has the right to disagree and not to contract, the defendant's conduct cannot be considered as a fault. The defendants had to bear the losses, because the works were done to meet their special requirements, and was prima facie for their **benefit**, not for the one of the landlords. Furthermore, they undertook to pay for the alterations and must be bound by their undertaking when the matter goes off **without the fault of either side**.[53]

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[49] At 432, 433.

[50] At 434.

[51] The plaintiffs didn't change their stand during the negotiations but only insisted on their initial refusal to give the defendants an option to purchase the premises.

[52] (1954)1 Q.B. 428, at 435, 436. Beforehand, Denning L.J. had excluded that the plaintiffs could sue out of a completed contract since the works were interrupted. They could neither sue for damages for breach of contract since there was no contractual obligation that the defendants had broken. Finally, they could not claim the money as being paid on request, because they didn't request the plaintiffs to pay money but merely wanted to pay for the alterations on completion of the works.

[53] (1954) 1 Q.B. 428, at 436 - 437

b) Consideration

Bearing in mind the very similar case of *Jennings & Chapman Ltd.* the incoherence between the arguments in both cases become apparent.[54]

First, in both cases the future tenants agreed to pay for the alterations that they had requested. When considering these agreements independently from the other circumstances, there is no reason to distinguish between the two cases, because in both of them the fundamental reason for the agreement had changed with the failure of the deal. It seems to be rather the conduct of the respective parties that determines who has to pay for the works done precontractually.[55] In *Jennings & Chapman* the reason for the failure rooted in the sphere of the plaintiff and in *Brewer Street* in the sphere of the defendants. Instead of blurring the true reasons for liability one should discern a logical reasoning when and on which legal ground there is liability for precontractual costs. If the parties made any arrangements with regard to the sharing of cost, these arrangements can be analysed with the help of classical contract law: Was it a fully binding agreement?[56] Was it subject to a - valid - condition? Only if there is no binding agreement with regard to precontractual costs, the problem of a possible legally imposed precontractual liability arises.

A second contradiction is the different handling of the allocation of the benefit. In *Jennings & Chapman* the plaintiffs were considered to benefit from the alterations, because they were in possession of the premises. Despite the fact that the situation was the same, the contrary was decided in *Brewer Street,* where Denning L.J. argued that the work was done for the benefit of the defendants, because they had requested the alterations.[57] Since in both cases the defendants requested the alterations and in both cases these alterations stayed with the plaintiffs, there is no objective reason to distinguish between them. Alterations on the premises of a prospective lessor can either enhance the value of his property. Then there can be a benefit on his side. Or it can be of no objective or subjective use for the lessor and, consequently, doesn't benefit him.

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[54] A. Burrows, *supra* n. 16, at 297.

[55] (1954) 1 Q.B. 428, at 433.

[56] This can only apply if it is an independent settlement of the responsibility to pay for precontractual costs. English law does not acknowledge an agreement to negotiate, *Regalian Properties plc* v. *London Dockland Development Corp.*, All ER (1995) 1, 1005, at 1015, *Walford* v. *Miles* (1992) 2 W.L.R. 174, H.L. at 179 - 81.

[57] (1954) 1 Q.B. 48, at 437. Furthermore, in *Brewer Street* the plaintiffs were the owners of the premises, whereas in *Jennings & Chapman* the plaintiffs were only lessees, thus, their property could not even have been enhanced.

3. *William Lacey (Hounslow) Ltd.* v. *Davis*[58]

In this case the defendant was the owner of premises which were destroyed during the war. He wanted to rebuild the property and invited builders to tender for rebuilding. The plaintiffs submitted the lowest tender and they were then led to believe that they were going to receive the contract. In the following one and a half years, the plaintiffs did considerable work on plans and estimates for the construction upon the request of the defendants, who used part of the estimates to negotiate with the War Damage Commission the 'permissible amount' for their premises. As a result of the estimates and other information provided by the plaintiffs, the amount receivable by the defendant from the War Damage Commission was substantially increased. The defendants later sold the premises and no contract for the rebuilding came about. The plaintiffs sued successfully for the expenses they had made.

a) Reasoning of the judgement

The considerations that led the court to grant the claim were that according to usage and custom the work, that the plaintiffs had done, **exceeded the normal work** which a builder performs gratuitously when asked to submit a tender.[59] The work was carried out only in the **mutual belief** that the plaintiffs would get the contract and their expenses would then be absorbed in the contract price. Furthermore, the defendants **benefited** from the plans and estimates the plaintiffs made, because a much higher 'permissible amount' was agreed to by the War Damage Commission, and this increased the price for which the house was sold.

Therefore, the court implied a promise by the defendant to pay a reasonable remuneration – a *quantum meruit* - in respect of such extra work.[60] Barry J. argued that the action for *quantum meruit* was not any longer a purely contractual claim but had nowadays been extended to quasi-contractual relationships. In quasi-contractual cases the courts look at the true facts and ascertain from them whether or not a promise to pay should be implied, irrespective of the actual views or intentions of the parties at the time when the work was done or the services rendered.[61]

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[58] (1957) 2 All ER 712.

[59] At 716, F. Logically the judge had clarified beforehand that usually when a builder tenders for certain work there is no implication that he will be paid for the work. He undertakes the work as a gamble and can only hope to recover some of his tendering costs out of the profits of contracts that he gets for successful tenders, at 715, I.

[60] (1957) 2 All ER 712, at 719, I.

[61] At 717, D, E.

Having looked at the circumstances of the case, Barry J. found that a promise to pay for the services must be implied. He said that he couldn't see any valid distinction between work done which was to be paid for under the terms of a contract erroneously believed to be in existence[62] and work done which was to be paid for out of the proceeds for a contract which both parties erroneously believed was about to be made. In neither case the work was to be done gratuitously and in both cases the party from whom payment was sought requested the work and obtained the benefit of it. In both cases the parties only wanted to pay for the work under the supposed contract or as part of the total price. In both cases the law implies an obligation to pay if the beliefs of the parties are falsified.[63]

b) Consideration

The new criterion for precontractual liability that has to be noted is the extent of the plaintiff's work, which exceeded the normal effort of a bidder. Apart from that, the decision confirms that the defendant's request and his benefit from the works are gauges for liability.

The legal foundation of an 'implied promise' into which these considerations are embedded is, however, a little difficult to comprehend. An 'implied promise' in English law is the 'fiction which the law creates to render one liable on contract theory so as to avoid fraud or unjust enrichment' and must not be established by reference to inward intentions as inferred from overt acts of the parties.[64] Hence, despite the confusing word 'promise' it is not a contractual but merely a quasi-contractual claim and as such part of the law of restitution and imposed by law when there is unjust enrichment.[65]

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[62] That refers to the case of *Caven-Ellis* v. *Canons Ltd.* (1936) 2 All ER 1066, at 1073 Greer L. J. held that the defendants P had to pay a *quantum meruit* for work that was done under a void contract.

[63] (1957) 2 All ER 712, at 719, F - H.

[64] H. C. Black, *Black's Law Dictionary*, (6th ed.) 1990, at 755; B. A. Garner, *A Dictionary of Modern Legal Usage* (1987), at 279 - 80. 'Implied' - correctly defined – means presumed to exist with reference to inward intentions or motives as inferred from overt acts: E.R.H. Ivamy, *supra* n. 41, at 132. This would be the meaning a continental lawyer would give to an 'implied promise', but in English law the word 'imply' got the meaning 'to infer', and hence, liability can be imposed also when it disrespects the intention of the parties, see again: B. A. Garner, this n. at 280.

[65] A. Burrows, *supra* n. 11, at 233 – 34; P. Birks, *supra* n. 17, at 29. Already 1952 an author stated, that the quasi-contractual obligations 'have nothing whatever to do with contract', P.H. Winfield, *The Law of Quasi-Contracts*, London 1952, at 2. It is only called quasi-contractual because the parties come together in the context of apparently concluding a contract. It is an 'implied-in-law' contract where the parties failed to make a promise and the law regards it as justified to hold one liable: H.C. Black, *supra* n. 54, at 1245; B. A. Garner, *supra* n. 54, at 458, 279 - 80.

Barry J. didn't refer to the three requirements of a claim for unjustified enrichment, but they could be discerned from his reasoning.

He states that the defendant, Davis, has benefited from the work the plaintiff has done, having received a higher purchase price for his house. As services and works cannot be physically restored, the appropriate measure of restitution is a reasonable amount that the plaintiff deserves for his efforts, i.e. a *quantum meruit*.[66] We should notice, however, that the court regarded the higher purchase price as the defendant's benefit but granted as restitution a *quantum meruit* for the works. This is inconsistent, since – in order to be 'restored' - the benefit and the matter of the restitution must substantially be the same.[67] The higher purchase price was merely an indirect result of the defendant's benefit, but not the benefit itself. Directly, he received the plans and estimates, the measurable benefit of which is their value, i.e. the amount that he would have had to pay for them.

Furthermore, it is obvious that the benefit was received on the expense of the plaintiff, who was the one who undertook the estimates and plans without any monetary reward.

Lastly, Barry J. substantiated why the enrichment was unjustified when basing his reasoning on the fact that the plaintiff had done an amount of work which exceeded by far what a competitor would ordinarily invest for a bid. Plus, this work was requested by the defendant and both parties had a mutual understanding that the plaintiff would be rewarded through the contract price. Under these circumstances the defendant could not expect the works to be gratuitous, even though, a bidder can usually not claim the costs that he incurs to submit a tender.[68] When justifying his decision with an analogy to situations where the contract is void,[69] the judge disregarded, however, that the confidence that a party has in a void contract is more justified than the one in an only envisaged contract. In the latter situation the plaintiff must know that there is still a material insecurity about the future existence of the contract. Except that this insecurity can be extremely minimised by the defendant's conduct.

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[66] *William Lacey (Hounslow) Ltd.* v. *Davis,* (1957) 2 All ER 712, at 719; Goff & Jones, *supra* n. 7, at 18, 19 - 21; A. Burrows, *supra* n. 11, at 237, 239; P. Birks, *supra* n. 17, at 266 - 67, 272 - 76.

[67] One has to be careful in defining by which benefit exactly the defendant was enriched and only this benefit can justifiably be restored: P. Key, *supra* n. 20, at 578 – 579.

[68] *William Lacey (Hounslow) Ltd.* v. *Davis,* (1957) 2 All ER, 712, at 719.

[69] *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712, at 719 F - H. Since *Craven-Ellis* v. *Canons Ltd.* (1936) 2 All ER 1066 there is a valid claim for a *quantum meruit* for work done under a void contract.

4. *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council*[70]

This Australian case concerned a plaintiff who successfully tendered for the development project of the defendant. Under the anticipated contract the plaintiff would take a building lease of a large and valuable site to construct a huge new civic centre. Sabemo then invested a great deal of time and expertise over a three-year period, in making and revising plans and models, attending meetings etc. Some large issues still remained under negotiation when the defendant decided to abandon the whole project. The reason for the abandonment was a new proposal by a council member for a far less ambitious scheme which the defendant then decided should be reviewed and reported on by the plaintiff. The plaintiff insisted that the basis for such further co-operation must be clarified, since its initial tender had already been accepted and was supposed to deliver the content of the envisaged contract. Following to that the defendant dropped that initial scheme. During the time of planning the parties had been in close co-operation and much of the detailed work was done at the express request of the council.[71] Sabemo was allowed to recover the cost of their expert input, excluding items which the judge, Sheppard J., thought had been incurred solely at their own interest and at their risk.

a) Reasoning of the judgement

The court held: 'Where two parties proceed upon a project on the joint assumption that a contract will be entered into between them, and the first party does work beneficial for the project, and thus in the interest of both parties, which work the first party would not be expected, in other circumstances, to do gratuitously, the first party will be entitled, by operation of law and notwithstanding that the parties did not intend, expressly of impliedly, that such obligation should arise, to compensation or restitution from the second party if the latter unilaterally abandons the project for reasons pertaining only to himself, and not arising out of a disagreement as to the terms of the proposed contract between the parties.'[72]

Sheppard J. clearly said that this was not a case of unjust enrichment, but one based on the newly emerged **principle** that – under the before-mentioned circumstances - an obligation to pay is implied by law.[73] The circumstance that led the judge to decide that the plaintiff was entitled to

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[70] (1977) 2 NSWLR 880.
[71] At 880 G.
[72] At 902 – 903.
[73] At 897 E; at 898 A and 899 F – 900 B.

recover was the fact that the defendant deliberately dropped the proposal. Even though, he may have had good reasons those reasons had nothing to do with the plaintiff, who in good faith, had assiduously worked towards the desired contract. Hence, the judge imputed a degree of **fault** to the defendant despite the principle of the freedom to contract - to break off negotiations at any time.[74] He underpinned this finding with the interpretation that the plaintiff would never have been prepared to incur these expenses had he thought that the defendant might change his mind.[75]

With regard to **benefit** the judge found that it wasn't necessary to establish that the defendant had received a benefit. Since the work was done in order to put the parties into a position to contract it was sufficient that it was beneficial for the project, and thus, in the interest of both parties.[76]

b) Consideration

This is the first decision where a judge decided that there must in principle be restitution when negotiations fail.[77] And it is also the first decision in which it was clearly said that the cause for liability lies in the reason for which the negotiations failed.

The other important outcome of the decision is the superfluity to establish a benefit. Therewith, the judge excludes the principle of unjustified enrichment as the ground for restitution.[78] He probably considered that it would have been very difficult to argue that the defendant had benefited. The work didn't bring about an outcome, and even if regarded as a pure service it wasn't done for the defendant but in a mutual interest.[79] Nevertheless, he regarded the case as deserving so that he found that the benefit cannot be a necessary requirement for liability.

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[74] At 900 E - F. He referred to the *Brewer Street* case to give some precedent to his view of seeing the defendant at fault.

[75] At 901 C. Sabemo took the risk that the negotiations could fail because of a failure to resolve the outstanding problems, but proceeded on the basis that there would be no unilateral withdrawal from the negotiation table, at 902-903.

[76] At 902 D – 903 A. Sheppard J. did not distinguish the case of *William Lacey* since he interpreted that there the judge's argument of the defendant's benefit merely supported the decision. The essence of the decision having been that both parties proceeded upon a joint assumption that a contract would be let.

[77] J. Mannolini, *supra* n. 20, at 115: it might be the extension of existing contractual or equitable principles or laying down a new and *sui generis* principle. I would suggest rather that Sheppard J. regarded it as a *sui generis* principle based on equitable principles inherent in the law of restitution that he found already in existence and merely formulated. At 898 he referred to the existing 'promise to pay implied' by law, stated that the previous cases had been decided on basis of that principle and then formulated it for precontractual dealings.

[78] P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 145 says that the basis of liability cannot be restitution if one resigns to the requirement of enrichment.

[79] According to P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 143 the application of the principle of free acceptance would have led to the finding that the council had received a benefit: Council had accepted the work in the knowledge of the basis on which it was done, and could, therefore, not argue 'Not valuable because not chosen'.

The judge also added the momentum of the plaintiff's **trust** into the defendant's conduct when he interpreted that the plaintiff would not have incurred the expenses had he thought that the defendant might abandon the negotiations. One could conclude that the defendant is at fault, because he disappointed the plaintiff's trust when breaking off negotiations without good reason. Liability then comes near to be based on disappointed trust, i.e. good faith.[80] It seems also to be more honest to aver that the restitutionary 'implied by law promise'[81] is rather founded upon the abuse of the plaintiff's confidence. On the other hand Sheppard J. relinquished the benefit – a notion logically indispensable to argue restitution, i.e. that something has to be 'restored'.[82] As content of the plaintiff's claim he names 'restitution or compensation'.[83] As a result, the basis for liability is inherently unclear. Even though, he says that 'a principle' for liability has emerged, he fails to ask why the law should impose liability under the said circumstances. The factual circumstances themselves cannot suffice to raise a principle, because they leave open the basic questions: Why can the plaintiff not be expected to do the work gratuitously? Why is it under the foregoing circumstances regarded as fault to break off negotiations, although, there is no legally binding agreement? Sheppard J.'s principle doesn't give a legally admissible conviction and reason for liability.

5. *Regalian Properties plc* v. *London Dockland Development Corp.*[84]

In *Regalian* v. *London Dockland*, the plaintiffs offered to undertake the residential development of land situated in London's former docks. The defendant (LDDC) was a corporation created under governmental plans to regenerate that area and was the owner of the respective land. On the 25 July 1986 the defendant accepted Regalians offer 'subject to contract, the district valuer's certificate of market value' and to the scheme 'achieving the desired design quality and the obtaining of detailed planning consent'. Extensive delays in concluding the contract occurred during 1986 and 1987.

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[80] For that interpretation see also: G Virgo, Anticipatory Contracts - Restitution Restrained, *CLR* 1995, 243, at 246; J. Mannolini, *supra* n. 20, at 115; A. Burrows, *supra* n. 16, at 298.
[81] A. Burrows, *supra* n. 11, at 233 – 34; P. Birks, *supra* n. 17, at 29; H.C. Black, *supra* n. 54, at 1245; B. A. Garner, *supra* n. 54, at 458, 279 - 80.
[82] P. Birks, in. A. Burrows (ed.), *supra* n. 30, at 145.
[83] (1977) 2 NSWLR 880, at 903.
[84] All ER (1995) 1, 1005.

First, the defendant persuaded Regalian to procure further designs from two specific firms of architects. Secondly, the parties needed to obtain detailed costing for the purpose of determining the sale prices of the units to be built. Thirdly, the defendant faced difficulties in securing vacant possession of the whole of the land which was necessary for the building process. And fourthly, the market values of residential property underwent a wide fluctuation, so that the offer that Regalian had initially made became blatantly uneconomical.

The parties entered into further negotiation to readjust the terms of the prospective contract to these fluctuations, but they came to nothing. No contract was concluded.

The plaintiffs sought recovery for their expenses of over 3 million Pounds representing fees which they had paid to professional firms in respect of the prospective development.

Rattee J. dismissed the action.

a) Reasoning of the judgement

Rattee J. distinguished the previous cases on that matter[85] from the present one as having different factual circumstances.

The first distinction he made was about the **character of the work** that the plaintiffs claim recovery for. Whereas in *William Lacey* the plaintiffs had done work for some 'extraneous or collateral purpose'[86], the expenditure of the plaintiffs in the present case was either for the purpose of satisfying the requirements of the proposed contract or of putting Regalian into a position of readiness to start the development.[87]

Secondly, the judge expressed his view that LDDC had not received a **benefit** from the work done by the plaintiffs. Rattee J. held that the value of the defendant's property was not enhanced, since it did not own any copyrights in the designs, so that it couldn't have used them itself or enabled any other developer to use them.[88]

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[85] *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712; *Sabemo Pty Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880 and *Marston Construction Co Ltd.* v. *Kigass Ltd.* (1989) 15 Con LR 116 (Canadian case).

[86] Namely to enable the defendant to negotiate a claim to the War Damage Commission, (1957) 2 All ER 712, at 716.

[87] *Regalian Properties* v. *London Dockland Development Corp.* All ER (1995) 1, 1005, at 1017 - 18, 1020 and 1023. The same distinction is made towards the case of *British Steel Corp* v. *Cleveland Bridge and Engineering Co Ltd.* (1984) 1 All ER 504, where the plaintiff undertook the work which would have been owed under the envisaged contract, which then failed. Hence, that was an accelerated performance of the contractual obligation, see Lord Goff J. at 511. In *Regalian* it was merely preparatory work.

[88] All ER (1995) 1, 1005, at 1018, 1022.

Thirdly, the judge held that the **reason** for the breakdown of the negotiations between Regalian and LDDC was their inability to agree on the terms of the intended contract, namely the price. It was not because one party 'unilaterally decided to abandon the project'.[89]

Fourthly, the work which was done by Regalian in connection with the contract would not have been paid for by LDDC.[90] LDDC's only obligation would have been to grant the building lease.[91] Accordingly, Regalian didn't expect to be rewarded through the contract price itself but only later through the profit they could make by leasing out the residences.

As a conclusion Rattee J. stated that even if English law of restitution shall be flexible and capable of continuous development, it cannot overcome the express agreement of the parties to undertake preparatory work 'subject to contract'. As the parties admitted, this term was used in its usual sense and, accordingly, the parties 'accepted that in the event of no contract being entered into, any resultant loss should lie where it fell'.[92]

b) Consideration

The judgement is convincing in its result, although, it doesn't offer new perspectives on the law of restitution and how to deal with cases of precontractual liability. Rattee J. merely applied precedence but no principle to base the claim on.[93] It is true, that the judge named as the possible basis for liability the law of restitution, but restitution is merely a generic term for relief which is granted for an unjust enrichment. The requirements for a successful restitutionary claim stay completely unclear, since Rattee J.'s purely negates Regalian's arguments and doesn't refer to the requirements of an unjust enrichment. Thereby, he obscures the jurisprudential motivation for his decision.[94]

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[89] At 1020.

[90] As in *Sabemo* (1977) 2 NSWLR 880, at 880: the anticipated project would have been financed wholly by the developer.

[91] All ER (1995) 1, 1005, at 1022.

[92] At 1024.

[93] Also a principle will be refined by case law, but at least it offers a legally convincing ground for relief: M. McInnes, *supra* n. 15, at 523.

[94] P. Key, *supra* n. 20, at 578.

(1) Benefit

Rattee J. concluded correctly that there was no benefit, although, his reasoning doesn't reflect the dogmatic concerning the notion of benefit, and consequently, seems legally rather unfounded.[95]
Since LDDC didn't receive money or any other corporeal item or right, it could as a benefit merely have gained the saving of the expense of paying for the designs itself[96] or it could have received the enhancement of its property's value.
With regard to the saving of expenses it is submitted that LDDC could 'subjectively devalue' this objective benefit.[97] LDDC would never have paid for the plans and designs, because one of their requirements for the building contract was that the bidder undertakes to provide appropriate plans and designs. Hence, they would not have incurred that expense in any case. It was for them the saving of an unnecessary expense – a controvertible benefit - and as such didn't enrich them.
Furthermore, the property value was not enhanced since the defendant didn't receive the copyrights of the plans and design and, consequently, couldn't use them to sell the land at a higher price.[98] There is already no objective benefit.[99]

(2) Unjust ?

Several considerations led Rattee J. to believe that it wasn't unjust for Regalian to bear the costs alone, although, he didn't apply any of the established unjust factors.
First, the judge concluded from LDDC's acceptance of Regalian's bid 'subject to contract', that the parties were at any time free to back out of the arrangement, and as a result, Regalian incurred the preparatory costs at its own risk.[100] The difficulty with this argument is, however, that it assumes that the whole dealings between Regalian and LDDC were based on a legal nothing. To accept Regalian's tender 'subject to contract' apparently meant that the acceptance – after all constituting element of the envisaged contract – would only receive binding force, when a formal

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[95] G. Virgo, *supra* n. 80, at 244; J. Mannolini, *supra* n. 20, at 113; P. Key, *supra* n. 20, at 577 - 8.
[96] P. Key, *supra* n. 20, at 577 - 8.
[97] P. Key, *supra* n. 20, at 578.
[98] Rattee's first argument - that there is no benefit because the property values had fallen so that no-one would wish to develop LDDC's land, and consequently, the development plans were ultimately worthless - is wrong. This is an event subsequent to the receipt of the plans, and therefore, only relevant as possible defence, i.e. change of position but not for the benefit: G Virgo, *supra* n. 80, at 244.
[99] For objective benefit see again: A. Burrows, *supra* n. 16, at 8; P. Birks, *supra* n. 17, at 109; Goff & Jones, *supra* n. 7, at 16 – 17.
[100] (1995) 1 All ER 1005, at 1009 and 1024.

contract would be concluded.[101] Consequently, accepting the offer at first, had no legal effect whatsoever,[102] especially as English law denies that there can be an agreement to negotiate in good faith.[103] But can this mean that LDDC didn't undertake any obligation, particularly having regard to the long period of negotiations and the immense costs? The previous case law and legal reasoning opposes such a finding. In all of these cases it was clear, that the parties would conclude a binding agreement only after successful negotiations and preparation.[104] Nevertheless, the courts rightly found that the relationship and legitimate expectations of the parties can be such that the defendant is liable when he abandons the negotiations for no good reason.[105] Hence, the 'subject to contract' condition can be overcome and is no good reason to deny liability.

Secondly, Rattee J. argued against liability with the fact that Regalian's work didn't exceed what was due as preparatory work according to LDDC's conditioned acceptance.[106] One could assume that the more remote the connection between the services performed and the anticipated contract is, the more likely it is that the plaintiff has a reasonable and enforceable expectation of payment.[107] This argument corresponds with the 'principle of free acceptance' and 'failure of consideration': As long as the work is usual for preparing a bid the defendant can accept those services without impliedly promising to pay for them.[108] This is, nevertheless, a difficult finding as it will be impossible to determine exactly when a service is remote enough to justify that the defendant has to pay his share. The agreement of the parties during negotiations will surely play a role, as it did here, [109] but also the character of the work and the amount of the costs.

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[101] That is like saying: We will only contract, when we will have concluded a contract.

[102] S.N. Ball, Work Carried Out in Pursuance of Letters of Intent - Contract of Restitution?, *LQR* 99 (1983) 572, at 572; as a letter of intent it merely memorialises the substance of their agreement at this stage and provides an impetus to consummate the bargain: W. H. Holmes, The Freedom not to Contract, *Tul. L.R.* 60 (1986) 751, at 777.

[103] *Regalian* (1995) 1 All ER 1005, at 1015; P. Neill, A Key to Lock-Out Agreements?, *LQR* 108 (1992) 405, at 408 - 409.

[104] See only *Sabemo* (1977) 2 NSWLR 880, at 880 and *William Lacey* (1957) 2 All ER 712, at 713.

[105] R Brownsword, 'Good Faith in Contracts' Revisited, *Current Legal Problems* 49 (1996) 111, at 131; W. H. Holmes, *supra* n. 102, at 777, 784: a letter of intent shouldn't by itself be binding, but at least the parties undertake to bring the negotiations forward, i.e. not to unjustifiably walk away from the bargain.

[106] (1995) 1 All ER 1005, at 1008: "...has accepted your company's offer for this site, subject to....your scheme achieving the desired design quality...".

[107] P Key, *supra* n. 20, at 579.

[108] Every bidder is expected to bear the costs for his tender himself: *William Lacey* (1957) 2 All ER 712, at 715, 716.

[109] In this case it seems unrealistic to regard Regalian's work as not excessive: no reasonable bidder would incur costs of over 3 million pounds without trusting that a contract will come about. Accordingly, the works were excessive despite the parties' agreement about which designs Regalian has to provide in order to satisfy LDDC.

Thirdly, Rattee J. referred to the reason for the failure of the negotiations as an element against LDDC's liability. The deal went off because of a change of circumstances and the simple failure of the parties to agree, which couldn't be attributed to LDDC. This confirms *Sabemo's* decision, that the conduct, and accordingly, disappointed trust is a reason for liability.[110]

Lastly, the fact that Regalian would have paid for the preparatory costs in any case, is not a valid argument. Even though, LDDC wouldn't have participated in the costs, Regalian would never have incurred them, had it not expected to be rewarded by receiving the contract. This very same argument operated in favour of liability in *Sabemo*, since the unfounded abandonment of the negotiations disappointed that expectation.[111] The true reason against liability was that Regalian's expectation was not disappointed by LDDC unilaterally since the parties failed to agree on the terms of the contract.

(3) Conclusion

The first difficulty for Reglian's claim under restitution was to establish LDDC's benefit. It would have been much easier for them to argue that they sought recovery for reliance losses.[112] Regalian undoubtedly suffered losses when incurring unrewarded expenses in preparation for a contract which they never entered into. Obviously, the step that Sheppard J. made in *Sabemo* – relinquishing the benefit – has not been taken in English law. English law also doesn't provide any other protection during precontractual dealings apart from tort, which was evidently not viable in this case. Therefore, Regalian was limited to the law of restitution which requires a 'benefit'.

6. Conclusion

Adjudication for precontractual liability was from the outset based on the 'implied-by law promise', thus, on the contemplation to grant restitution for an unjust enrichment in a contractual context – i.e. a quasi-contractual claim. While restitution in such cases contains the *quantum meruit* for services provided, it still requires that the defendant received a benefit. *Quantum meruit*, however, means rather that the plaintiff deserves under the circumstances a compensation for his effort, not necessarily that the defendant was enriched. Therefore, it should be carefully considered, whether 'benefit' is a necessary requirement, as Sheppard J. did in *Sabemo*.

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[110] R Brownsword, *supra* n. 105, at 130 – 131.
[111] (1977) 2 NSWLR 880, at 880 and 901 C.
[112] P Key, *supra* n. 20, at 578.

Maybe the true justification to give or deny a claim is that the plaintiff's confidence in the truthful conduct of the defendant towards the conclusion of a contract was or was not disappointed. All of the decisions were at least partly based on the reason for which the negotiations failed.[113]

Also, in all of the decisions the plaintiffs suffered heavy losses when firmly and justifiably expecting a contract to eventuate. The character of a loss, however, rather suggests an action in tort,[114] or maybe a quasi-contractual but not restitutionary claim for the compensation of efforts that would be unjustified to stay unrewarded.

The appropriateness of the law of restitution as a basis for these precontractual claims should, hence, be scrutinised by taking a closer look at the requirements and how these apply to the cases in question.

III. Critical analysis of restitution as a basis for precontractual liability

Having seen the difficulty and variety of cases where negotiations are broken off, we must now examine how aptly the requirements of restitutionary claim apply to these cases.

1. Benefit

As was set out above, the benefit is a complicated requirement, that can be defined objectively or subjectively. In order to limit the 'subjective devaluation' of an objective benefit, the tests of an 'incontrovertible benefit' and of 'free acceptance, request or the bargained-for benefit' can be applied according to the circumstances.

a) Incontrovertible benefit

A benefit is incontrovertible when the defendant was saved a necessary expense or when he received an already realised or readily realisable gain.

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[113] In *Jennings and Chapman* the plaintiffs failed to provide the owners consent to the sublease: (1952) 2 T.L.R. 409, at 413: claim denied; in *Brewer Street* the defendant unilaterally abandoned the lease: (1954) 1 Q.B. 428, at 434: claim granted; in *William Lacey* the defendant sold the premises, and thereby, caused the negotiations to fail: (1957) 2 All ER 712, at 719, although, Barry J. didn't base his judgement on this argument, he denied the claim because the belief of the plaintiff in the conclusion of the contract was falsified; in *Sabemo* (1977) 2 NSWLR 880, at 903 A, and lastly, *Regalian* (1995) 1 All ER 1005, at 1020.

[114] P. Birks, *Restitution - The Future*, at 102; J. W. Carter, *Ineffective Transactions*, in: P. D. Finn (ed.), *Essays on Restitution*, at 226.

In cases of failed negotiations the plaintiff hardly ever tries to recover necessary[115] expenses. The plaintiff undertakes works for an anticipated contract. In such contractual dealings the defendant assumes expenses typically voluntarily acting within his freedom to contract.

Sometimes, preparatory services lead to an ascertainable gain of the defendant, see *William Lacey*, where the defendant had obtained a higher purchase price for his house. Consequently, this category, although, not explicitly confirmed by case law, can separate deserving cases where there is already an incontrovertible benefit.[116]

b) Free acceptance vs. Request vs. Bargained-for benefit

These tests forbid the defendant to argue that he 'subjectively devalues' the benefit. He either accepted instead of refused works where a reasonable person must have realised that the plaintiff expected to be paid for them or he requested them explicitly or bargained for them.

Again, we must look at the specific circumstances where negotiations flop.

(1) Applicability of the tests

In all of these cases the parties were in contact with each other and the plaintiff relied on the defendant's conduct when undertaking works. Consequently, the defendant - if he knows about the work - will usually have a reasonable opportunity to reject such undertakings, so that the test of 'free acceptance' is in principle applicable.[117] Nevertheless, the 'free acceptance' still requires that a reasonable person must have realised that the plaintiff expected payment for the services. This is where the core problem of precontractual liability lies. Generally, a bidder pays for his preparations himself and merely hopes to be rewarded through the profit of the anticipated contract.[118] As a result, the defendant will never expect to pay for the works as such. Yet, one could contend that the defendant must know that the plaintiff reasonably expects indirect payment through the contract price under specific circumstances. For example, when the defendant

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[115] There is dispute as to when an expense is necessary. Some think only legal necessities can qualify, see the cases of *Craven-Ellis* v. *Canons Ltd.* (1936) 2 K.B. 403; *Monks* v. *Poynice Pty Ltd.* (1987) 11 A.C.L.R. 637, others include also factual necessities, see: *Peel* v. *Canada* (1993) 98 D.L.R. (4th) 140, at 157 - 60; *Upton R.D:C.* v. *Powell* (1942) 1 All ER 220; and: Goff & Jones, *supra* n. 7, at 178; P. Birks, *supra* n. 17, at 120; A. Burrows, *supra* n. 16, at 124 - 5. P. Birks advocates the most liberal approach by disregarding only unrealistic and fanciful possibilities and finds guidance in the law which says what constitutes a 'necessary' to a minor or other person under an incapacity, P. Birks, *supra* n. 17, at 120 - 21.

[116] One must keep in mind, however, that even though there is no incontrovertible benefit, the tests of free acceptance, request and bargained-for benefit can still apply and establish a legal benefit.

[117] N. S. Ball, *supra* n. 102, at 575.

encouraged him to incur precontractual expenses and stirred the firm belief that a contract will surely be concluded the plaintiff expects that a contract will reward his efforts.[119] If one regards this indirect reward as 'payment' for the accepted services the 'principle of free acceptance' can logically be applied.

The same is true for the varieties of the stricter requirement where the defendant must have positively indicated that he is willing to receive and pay for the services in question. In most of the cases of precontractual dealings the defendant expressly requested the services and expected to pay for them[120] - at least under the anticipated contract[121].

(2) Appropriateness of the tests in failed negotiations

The characteristics of the cases of failed negotiations avail that there are two main problems when applying the tests of 'free acceptance', request and bargained-for benefit.

First, the tests can logically overcome cases where the defendant didn't even receive anything, which happens quite frequently with precontractual works. The interpretation of a benefit seems then rather distorted.

For example in the case of *Sabemo* P. Birks insisted that the principle of free acceptance would have established a benefit. He stated that the council had accepted Sabemo's efforts in the knowledge of the basis on which they were done, so that he could not say 'Not valuable because not chosen'.[122] Also the tests of request and the bargained-for benefit would come to the conclusion that the council benefited as he expressly requested Sabemo to undertake the works. As a matter of fact, the council neither received anything tangible nor did Sabemo confer services **to** the council, since it had a perfectly equal interest in the works.[123] Consequently, the tests themselves merely look at the defendant's conduct. The defendant is regarded as enriched, simply

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[118] *William Lacey* (1957) 2 All ER 712, at 715, 716; A. Farnsworth, *supra* n. 4, at 221.

[119] It is a different question whether the plaintiff's expectation of a contract is to be legally protected in view of the freedom not to contract.

[120] *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 T.L.R. 409, at 410; *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) Q.B. 428.

[121] *William Lacey Hounslow Ltd.* v. *Davis* (1957) 2 All ER 712.

[122] P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 143.

[123] The same is true for *Regalian*, where LDDC did not receive the plans and designs, nor a copyright of them, so that they also didn't increase LDDC's property value: (1995) 1 All ER 1005, at 1018 H. With regard to the plaintiff's interest in the works one has to distinguish: The person rendering a service, always has an interest in doing so, since she wants to be paid for them. There is, however, a further interest in *Sabemo* and *Regalian* where the plaintiff had an interest in the content of the work itself.

because he showed that he subjectively ascribes value to the services.[124] This cannot be true. In order to regard someone as enriched, there must at least be some positive accretion of wealth in his hands.[125] In cases of precontractual works this can be either a service which leaves the defendant with an end-product – e.g. designs and plans that enhance his property value -, or, a pure service - i.e. a service which does not produce an end product[126] - which is ministered to the defendant.[127]

Secondly, the tests pervert the order of the examination concerning unjustified enrichment. When applying the tests one will have to argue already about the justice of the enrichment.

Their investigation is based on the assumption that the defendant showed that he values the services in that he accepts, requests, bargains for them in the expectation to have to pay for them. For precontractual work, however, the plaintiff will normally not get payment but only the contract. Therefore, one could well assert that the defendant didn't value the service because he might have accepted or even requested it, but wasn't prepared to pay. He could expect the plaintiff to render services in preparation of the contract free of charge. On the other hand, the plaintiff could have incurred extraneous costs solely because he justifiably relied upon the defendant's conduct, which indicated that a contract would come about. When the defendant so

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[124] P. Birks, in: A. Burrows (ed.) *supra* n. 30, at 143.

[125] See A. Burrows, *supra* n. 16, at 8 – 9. In that regard the decisions of *Planche* v. *Colburn* is wrongly situated within the law of restitution. The defendant must at least have received something, for this view compare: Goff J. in *BP Exploration Co. (Libya)* v. *Hunt (No. 2)* (1979) 1 WLR 783, at 800. It doesn't seem useful to purport that the defendant has benefited if he didn't receive anything, even if the plaintiff fulfilled his respective obligation, see for such an approach the British Columbia Frustrated Contracts Act, s. 5 (4) 1974 BC Statutes, Ch. 37; J. Beatson, *The Use and Abuse of Unjust Enrichment*, at 40 - 1.

Also a merely subjective benefit can be a benefit, as long as it is received: M. Garner raised this point with the example of the extremely ugly painting of a house which objectively diminishes the value of the house: M. Garner, *Benefits - For Services Rendered: Commentary*, in: M McInnes (ed), *Restitution: Developments in Unjust Enrichment*, at 112. It is another problem to determine, what an objective benefit is: If the benefit has market value, P. Birks, in: Burrows (ed.), *supra* n. 30, at 129; if the benefit is of utility, J. Beatson, *supra* n. 125, at 30 - 1.

[126] Beatson distinguishes pure services from services that produce an end product. A freely accepted service which produces an end product provides a marketable residuum and can, therefore, be an enrichment. A freely accepted pure service - a musician performs, a window is cleaned -, however, cannot constitute an enrichment, because it doesn't leave a marketable residuum. J. Beatson, *supra* n. 125, at 23 - 24. This distinction was not well received and it can hardly be denied that also pure services can be of an objective as well as a subjective benefit to the defendant, see Goff & Jones, *supra* n. 7, at 22, Jones, *A Topography of the Law of Restitution,* in: Finn (ed.), *Essays on Restitution,* at 3 - 4 and the Australian case *Brenner* v. *First Artists' Management Pty Ltd.* (1993) 2 V.R. 221, at 257. E. McKendrick, *Frustration, Restitution, and Loss Apportionment*, in: A. Burrows (ed.), *Essays on the Law of Restitution* (1991), at 161.

[127] The benefit lies either in the end-product or in the value of pure services that the defendant received: E. McKendrick, in; A. Burrows, *supra* n. 126, at 161 and 163. He can either want to receive the services himself or direct that it is rendered to another person, in each case the benefit gets into the defendant's sphere.

causes the plaintiff to squander his efforts, can he then be entitled to argue that it was a merely precontractual service and he, therefore, didn't expect to pay? And what can the plaintiff rightly trust in: the conclusion of the contract or rather that the defendant will not unilaterally cause the negotiations to fail or that he will not be unrewarded even if the negotiations fail? This discussion is the core problem of whether it is 'unjust' to let the defendant receive the plaintiff's effort unrecompensed but it doesn't primarily concern the issue if the defendant was enriched.

c) Conclusion

It has been shown, that the notion of an incontrovertible benefit can be applied to the examined cases. The principle of free acceptance, of a requested or bargained-for benefit, however, proved to be too complicated in order to grasp a possible enrichment through works preparatory for a contract.[128]

The cases of *Sabemo* and *Regalian* demonstrated that a plaintiff can incur vast costs to prepare for a contract without the defendant being even objectively enriched. It doesn't seem justified to deny a claim, simply because no benefit accrued to the defendant. The same conclusion has been drawn in *Sabemo*.[129]

In many of the concerned cases the plaintiff undertakes preparatory works in the mutual interest of plaintiff and defendant to bring about the contract. If then the defendant abandons the negotiations, the reason for his liability is less the fact that he might unilaterally be enriched, than his breaking off without good reason. Furthermore, the expenses and efforts of the plaintiff being in vain appear to be rather a loss to him than a benefit to the defendant.

To conclude, the benefit should not be a requirement for liability.

A new approach could be the school of thought that treats these cases under the notion of an 'unjust sacrifice' as the pendant to unjust enrichment.[130] Their submission is that the plaintiff mustn't establish a benefit, but merely that he suffered a loss.[131] The reasoning in *Sabemo* already points in such a direction.

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[128] It is too complicated already in general when one tries to cover just subjective devaluation: S. Hedley, 'Unjust Enrichment' *CLJ* 54 (1995), 578, at 596.

[129] Rattee J.'s denial of the remedy in *Regalian* was mainly founded on other considerations than the lack of a benefit – i.e. on the reasons for the failure of the negotiations and the 'subject to contract' agreement.

[130] A. Burrows, *supra* n. 16, at 293.

[131] A. Burrows, *supra* n. 16, at 299: he contends that one can only promote an 'unjust sacrifice' as a cause of action, when advocating 'promissory estoppel' as cause of action. Since promissory estoppel – which prohibits the holder of a right to enforce his right, because he previously made his vis-à-vis rely on a non-enforcement – isn't accepted

2. At the Plaintiff's Expense

The enrichment must have been gained at the plaintiff's expense, i.e. either by subtracting wealth from the plaintiff or by committing a wrong against the plaintiff.[132]

For the cases of anticipated contracts that fail to materialise, mainly subtractive enrichment will have taken place. The plaintiff incurs expenses for the anticipated contract, for example by undertaking works, as in *Brewer Street* or by paying sums for plans for the prospective development project as in *William Lacey* and *Regalian*.[133]

There might be circumstances where the defendant was enriched by committing a wrong, for example when he fraudulently purports that he will conclude a contract, but truly isn't willing to do so.[134]

The cases of precontractual dealings are not particularly difficult to summarise under the requirement of the enrichment 'on the plaintiff's expense'. Some usual difficulties might come up, such as the question whether the enrichment must be 'ultimately' on the plaintiff's expense or merely intermediately[135] or whether the enrichment is 'at the plaintiff's expense' when it was gained from a third party.[136] Most of the cases, however, concern situations where the defendant blatantly benefited on the plaintiff's expense, his costs, works and services. Hence, this requirement is clearly applicable to the cases in question and doesn't pose conceptual problems.

3. 'Unjustified'

It was set out above that the possible unjust factors for failed negotiations are the failure of consideration and the free acceptance of the plaintiff's services and expenses. We must now examine how aptly these tests cover the cases in question.

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in English law as a cause of action, but merely as a defence, he sees no basis for 'unjust sacrifice'. But if one regards 'unjust sacrifice' as another variety of 'unjust enrichment', one doesn't need promissory estoppel to justify this remedy. When the reason for liability isn't the fact that the defendant received a benefit, but truly that he disappointed the plaintiff's trust, and thereby, caused the plaintiff's loss in an unjustified way, then the loss should be sufficient requirement for liability instead of a benefit.

[132] M. McInnes, in: M. McInnes (ed.), *supra* n. 17, at 30, 31 and 37.

[133] Compare Goff & Jones, *supra* n. 7, at 35.

[134] Hence, a case of misrepresentation, A. Burrows, *supra* n. 16, at 18.

[135] *Commissioner of State Revenue (Vict.)* v. *Royal Insurance Australia Ltd. C.L.R.* 182 (1994) 51, which is an example of how public authorities may pass their loss on to the taxpayer; J. Beatson, Restitution of Overpaid Tax, Discretion and Passing-On *LQR* 111 (1995), 375; see Goff & Jones, *supra* n. 7, at 35.
Some problems will never arise, such as the vividly discussed obstacle whether the breach of contract can be a civil wrong for which the defendant is regarded as being enriched 'on the plaintiff's expense', see M. McInnes, in: M McInnes (ed.), *supra* n. 17, at 39 - 41.

a) Failure of consideration

The failure of consideration constitutes an unjust factor, because what was promised to the plaintiff fails to materialise. Thus, the plaintiff's basis for incurring the expenses has been disappointed.[137]

Applied to anticipated contracts that fail to materialise, that means that the defendant has to give restitution to the plaintiff, because he has refused to perform his 'bargained-for' promise – namely to conclude a contract - which was the plaintiff's reason for rendering a benefit / sacrifice.[138]

The use of the 'total failure of consideration' - test confronts a conceptual difficulty[139] in these cases: Since the examined cases are all playing in the precontractual phase, there is no 'promised return', rather, the so-called promise of the defendant, never presented a binding engagement – freedom of contract.[140] It is, therefore, difficult to argue, that it is evenly unjust when the defendant doesn't perform something which he never promised in a binding way than it is when he fails to perform something he contractually bound himself to do. The counter-argument for this could be that it might not be a contractual promise, but still a precontractual bargain which must be respected as well.[141] Since the English law doesn't recognise a contract to negotiate, this is a very controversial finding.

It must be determined, when and in how far such a precontractual bargain can be regarded as a 'promise' equal to the consideration of a contract so as to justify a restitutionary claim. In precontractual dealings the parties must be aware that they can generally not rely on receiving a counter-performance, since they have the freedom not to contract. The plaintiff runs the risk that he undertakes his effort in vain.[142] Hence, the failure to reward the plaintiff's precontractual effort

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[136] Goff & Jones, *supra* n. 7, at 36 - 38.

[137] *Fibrose Spolka Akcyjna* v. *Fairbairn Lawson Combe Barbour Ltd.* (1943) A.C. 32, at 48; A. Burrows, *supra* n. 16, at 251, 253, 259 – 261.

[138] A. Burrows, *supra* n. 16, at 294; P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 114, see for the case of *Sabemo* P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 143.

[139] There is also other criticism about this theory, for example that it is traditionally only applicable to cases where the defendant received money, but not where he received goods or services, see P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 112.

[140] J. Carter, *Restitution and Contract Risk*, in: M. McInnes (ed.), *Restitution: Developments in Unjust Enrichment*, at 148.

[141] A. Burrows, *supra* n. 16, at 293.

[142] K. Liew, *Restitution and Contract Risk*, in: M. McInnes (ed.), *Restitution: Developments in Unjust Enrichment*, at 167.

cannot per se be regarded as unjust.[143] Only if there is further reason for the plaintiff to justifiably expect the defendant to conclude a contract, will his sacrifice be regarded as unjust.[144] This is where the difficulties with these specific cases reveal themselves. One problem is how to determine, when the defendant's conduct is such that a reasonable plaintiff should legally be allowed to trust that he will receive a counter-performance. As *Sabemo's* case showed, this can depend on the conduct of the defendant, of the plaintiff and also on the stage of the negotiations.[145] A second difficulty is to determine what the failed counter-performance is. In contractual cases the counter-performance is determined by the contract. In precontractual cases it could be the conclusion of the anticipated contract or merely to continue to bargain in good faith, i.e. that the defendant does not break off the negotiations without good reason.

All these difficulties are not addressed, if we simply apply the 'failure of consideration' as it now stands to cases of precontractual dealings by saying that the defendant refused to perform his 'bargained-for promise'. One should find some formula to limit and define when there is reasonable reliance into the 'consideration' in precontractual dealings.

b) Free acceptance

The principle of free acceptance is here applied in its second function. It is forwarded as an unjust factor, arguing that the defendant accepted the benefit / sacrifice while he had the opportunity to reject it in order to save the plaintiff from squandering his services.[146]

This principle faced much criticism.

The first is one of principle: it has been pointed out that it doesn't seem to be unjust not to pay a risk taker. If the window-cleaner cleaned the window in the mere hope to be paid for his effort, it might be shabby, but not unconscionable to refuse payment, because just the very risk, that the cleaner took, manifested itself.[147] Also in precontractual dealings the plaintiff is generally such a risk taker.

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[143] J. Carter, *supra* n. 140, at 148.

[144] P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 114. He suggests, that 'one can make a transfer on the basis that a contract shall come about'. This merely amends the definition of the 'failure of consideration'-test, so that it applies to precontractual cases. It does not, however, scrutinise, why it is justified that the plaintiff trusts that a contract will come about, hence, why it is unjust that the defendant keeps the benefit that he received without compensation.

[145] J. Carter, *supra* n. 140, at 149.

[146] P. Birks, in: A. Burrow (ed.), *supra* n. 30, at 111.

[147] A. Burrows, *supra* n. 16, at 316; G. Mead, Free Acceptance: Some Further Considerations, *LQR* 105 (1989), 460, at 463, identifies this acceptance of a risk as a principle of tort law.

Secondly, if we apply the principle to the cases of precontractual works the specific problems of these cases are not sufficiently accommodated. Even Birks, one of the biggest advocates for free acceptance, acknowledges that 'free acceptance' doesn't deal appropriately with these cases and adopts Burrows' view that the unjust factor is the 'failure of consideration'.[148] 'Free acceptance' doesn't work here, as it can not be regarded as unconscionable to request and receive services during precontractual dealings. Precontractual services such as a quote, an estimate or plan are commonly unpaid services. Generally, the plaintiff consciously runs the risk of rendering services unpaid when no contract is yet agreed to.[149] Further indicators must render the non-payment unjust, like for example the length of the negotiations, the extent of the services or a specifically promising conduct of the defendant. The principle, however, doesn't provide other clues than the mere acceptance to determine whether the defendant acted unconscionably and is, therefore, not applicable to the more complex cases of precontractual dealings.[150]

c) Considering the true reasons for liability

Neither the failure of consideration nor the principle of free acceptance give *per se* a comprehensible explanation why and when an enrichment /sacrifice in precontractual cases is unjust.

The governing idea is, that an enrichment is only unjust if there are circumstances that lead a reasonable plaintiff to legitimately believe that he will be rewarded for conferring the benefit / sacrifice unto the defendant precontractually.

Elements that have been decisive in the relevant cases, but were never associated with the 'unjust factor' are the following:

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[148] P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 113 - 5.

[149] Apart from the few cases, where the plaintiff can show, that the defendant is initially unconscientious, for example, when he initially planned to exploit the plaintiff's resources. A quote or estimate can be requested and is usually a free of charge service of the plaintiff, see P. Birks, in: A. Burrows (ed.), *supra* n. 30, at 115.

[150] J. Carter, in: M. McInnes (ed.), *supra* n. 140, at 149 finds that free acceptance is the right basis for restitution in these cases. He regards the defendant as a risk sharer from the moment on when he accepts the benefit without asking whether his conduct was unconscionable. The risk he shares is that no contract will be agreed. Being a risk sharer it is legitimate for society to impose liability. Probably the enrichment is regarded as 'unjust', because it would be unfair to leave the plaintiff alone with his expenses, since the defendant undertook to share the risk that their dealings fail. It seems, however, highly artificial to regard the defendant as a risk sharer just because he accepts a benefit. This is just an allegation, especially in the context of precontractual dealings, where it is highly controversial, when the plaintiff can legally be regarded as not having to bear the risk, that the negotiations fail,

- The parties must share the honest anticipation of the contract.[151] No plaintiff can reasonably expect that he will be recompensed for an effort that is motivated by his unilateral wish to achieve a binding contract. Furthermore, a reasonable plaintiff must know whether the defendant anticipates the contract as well or not. Only if there is some outward objectively promising conduct of the defendant can the plaintiff understand and trust that his negotiating partner shares the anticipation.

- The defendant must have requested the service or enticed the plaintiff in some other way to undertake the services or works.[152] A request or encouragement to undertake certain works can make a reasonable plaintiff believe that he is going to be rewarded for them.

- What the plaintiff undertakes must be work which exceeds what he would normally do during the negotiating process.[153] The works and expenses must be more than a quote or a simple inquest in the feasibility of the envisaged contract. Often, it will be determined upon the circumstances whether the work is extraneous or not. Indicators can be the amount of the costs, the period of negotiations or the agreements of the parties about the extent of precontractual services.

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alone, see K. Liew, in: M. McInnes (ed.), *supra* n. 142, at 167 - 8. Hence, this approach does not give a comprehensible explanation why the defendant has to pay restitution.

[151] *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409, at 412, *Watson* v. *Watson,* (1953) NZLR 266, at 272; *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) 1 Q.B. 428, at 436; *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712, at 719; *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880, at 902; *British Steel Corp.* v. *Cleveland Bridge and Engineering Co. Ltd.* (1984) 1 All ER 504, at 511; *Regalian Properties plc* v. *London Dockland Development Corp.* (1995) 1 All ER 1005, at 1015, 1024. K. Liew, in: M. McInnes (ed.), *supra* n. 142, at 167; J. Carter, in: M. McInnes (ed.), *supra* n. 140, at 149.

[152] *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409, at 413, *Watson* v. *Watson,* (1953) NZLR 266, at 273 (the defendant had invited, permitted and encouraged the plaintiff to render services); *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) 1 Q.B. 428, at 435; *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712, at 716; *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880, at 902; *Marston Construction Co. Ltd.* v. *Kigass Ltd.* (1989) 15 Con.LR 116, at 127; *British Steel Corp.* v. *Cleveland Bridge and Engineering Co. Ltd.* (1984) 1 All ER 504, at 511; *Regalian Properties plc* v. *London Dockland Development Corp.* (1995) 1 All ER 1005, at 1009 (Rattee J. accepts that LDDC encouraged Regalian to incur the expense, but didn't expressly request it. Later, the issue, whether a request is necessary to found a claim is not dealt with. Rattee J. restricts his argument to the lack of a benefit and his opinion that the work was merely preparatory).

[153] *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712, at 716 - 7; *British Steel Corp.* v. *Cleveland Bridge and Engineering Co. Ltd.* (1984) 1 All ER 504, at 511 Goff J. uttered that he work performed was work which would have been performed under the anticipated contract. Thus, the work is not any longer merely preparatory. *Regalian Properties plc* v. *London Dockland Development Corp.* (1995) 1 All ER 1005, at 1023 Rattee J. firmly stated that he considers the work done as merely preparatory in that it was geared at putting Regalian in a position to obtain and then perform the contract.

- Lastly, it has been looked at whether the defendant has been at 'fault' or responsible for the failure of the negotiations.[154] It surely is contradictory to regard someone as being 'at fault' for breaking off negotiations when he in principle has the freedom to negotiate, hence, to break off negotiations.[155] Accordingly, this can never be the only reason, why a defendant is liable. Only, if his previous conduct led the plaintiff to believe that he would not break off without good reason, can this be an argument for his liability.[156] A good reason for abandoning the negotiations can lie in the plaintiff's conduct, in the parties disagreement about the terms of the anticipated contract or in a change of outside condition – such as unforeseen price developments as in *Regalian*.

These were the decisive arguments for granting the plaintiff the action for unjustified enrichment. Not one single element has been sufficient to ground the claim but it is also not necessary that all four reasons prevail. Indispensable is, however, the fact that the defendant by some outward conduct led the plaintiff to believe that a contract would surely come about and didn't merely hope so. Otherwise the plaintiff would undoubtedly be a risk taker and would have to bear the costs if no contract eventuates so that his expenses were in vain. This does not alleviate, however, the problem to discern when the defendant showed such a behaviour during the gradual process of negotiation. Sometimes alone the request for the works during an advanced stage of negotiation can be enough.[157] Often, an assumption for defendant's enticing conduct will be fostered by the fact that the preparatory works are excessive compared to usual tendering services.

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[154] *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409, at 413 (no fault, but plaintiff himself only knew about the requirements of the anticipated lease and failed to receive consent), *Watson* v. *Watson,* (1953) NZLR 266, at 272 (states that the defendant was the one who 'repudiated' the understanding); *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) 1 Q.B. 428, at 432 (the defendants 'entirely on their own motion' decided not to go on with the lease); *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712 (there was no mention of fault, but it was held that the defendant led the plaintiff to believe that they would receive the contract and then the defendant unilaterally decided to sell the land instead of developing it); *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880, at 900 Sheppard J. held that he regards the defendant to be at fault for unilaterally and without good reason breaking up the negotiations.).

[155] Goff & Jones, *supra* n. 7, at 558.

[156] This consideration reminds rather of a promissory estoppel, although, English law only recognises this principle as a defence and never as an action to ground a claim on it. Goff & Jones, *supra* n. 7, at 559 - 60; G. Virgo, *supra* n. 80, at 245; P. Key, *supra* n. 20, at 579 - 80.

[157] Like in *Marston Construction Co. Ltd.* v. *Kigass Ltd.* where the fact that the defendant requested the services was decisive for the successful claim of the plaintiff, although, the parties had expressly submitted their future contract to the condition that the defendant would obtain enough insurance money.

Another indispensable element for liability is the 'fault' of the defendant for the failure of the negotiations. If the plaintiff contributed to the downfall it would be unjust if he was entitled to sue the defendant for losses that he himself caused. Also, when outward reasons cause the negotiations to fail, one cannot hold the defendant responsible. In that case only the risk of unsecured precontractual dealings manifested itself and not the risk of a one-sided backing out of the negotiations, which the defendant had excluded by his 'promise' to continue negotiating.

d) Conclusion

These elements for liability can aptly be considered within the notion of 'failure of consideration'. First, one will have to analyse whether the defendant 'promised' anything to the plaintiff through his conduct or expressly, secondly, which promise he made - to honestly endeavour the conclusion of a contract ? -, and under which conditions or premises, and lastly, if the defendant failed to fulfil his promise or if other reasons caused the unsuccessful ending of the deal.

IV. Conclusion

The remedy of unjust enrichment is inappropriate when one insists on the benefit. The requirements 'at the plaintiff's expense' and the unjust factor accommodate the special problems that the precontractual character of the cases poses. Nevertheless, the forcing of these cases under the law of restitution obscures why and when there could be liability.

We saw that the defendant should be liable only when he raised the plaintiff's trust into the conclusion of the contract, and thereby, caused him to incur expenses that exceed what a normal bidder would perform. Then he must disappoint that anticipation by causing the negotiations to fail without having a good reason for his abandonment.

These are elements which are alien to the law of restitution. The defendant is mostly not enriched, but the plaintiff incurred losses and wasted his efforts. Then nothing must be 'restored' to him. He seeks damages or compensation. Furthermore, the causation of the expenses and of their futility played an important role in all of the cases. Restitution doesn't look at causality as such. The causation is only indirectly looked at, when asking whether the enrichment was 'at the plaintiff's expense' and if the defendant failed to perform his promise.

As a result, the law of restitution, and in particular, the principle of unjustified enrichment don't present a perfect basis for liability.

The judges in the presented cases based their decision on the mutual anticipation of the contract on the request for the works and the reason for the failure of the negotiations. These deliberations reveal that the plaintiff is protected, when his trust into the defendant's conduct was disappointed.[158] Accordingly, English law guards for 'good faith' during negotiations, although, it is most sceptical towards the adoption of a doctrine of good faith for fear that it produces an unanalytical incantation of personal values and invites judges to abandon legally reasoned decisions.[159] The examination of the English decisions showed, by contrast, that the judgements are unanalytical and insufficiently legally founded rather for the lack of clarity about the rationale of liability. To accept that the protection of 'good faith' stands on the beginning of liability could explain these judgements. It would reflect the parties' expectations instead of distorting them – which would be the result of a strict denial of liability in application of the freedom of contract.[160] An example which should encourage an English doctrine of good faith is the Israeli law. Stemming from English common law it adopted an explicit duty to negotiate in good faith in 1973. The adoption of the good faith doctrine had no detrimental consequences and became an apt tool to achieve reasonable and just decisions.[161]

C. Negligent misrepresentation

Another remedy which is used to recompense the negotiating partner for losses when the contract fails to materialise is the tort law. In particular, the tort of negligent misrepresentation applies to these cases.

In South Africa the only case of precontractual liability for failed negotiations was dealt with under negligent misrepresentation. I will evaluate the merit of the tort of negligent misrepresentation for precontractual cases with the help of this case and South African law of negligent misrepresentation.

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[158] R Brownsword, *supra* n. 105, at 131.

[159] *Walford* v. *Miles* (1992) 1 All ER 453, at 460 – 461; R Brownsword, *supra* n. 105, at 113.

[160] R Brownsword, *supra* n. 105, at 125, 127 – 128, 129; M Furmston, Is There a Duty to Negotiate in Good Faith? *LQR* (1998) 362, at 363.

[161] A M Rabello, *supra* n. 4, at 59; N. Cohen, Good Faith in Bargaining and Principles of Contract Law, *Tel Aviv Univ. Stud. In Law* 9 (1989), 249, at 276 – 277, 310.

I. Murray v. McLean N.O.[162]

The facts of the case are as follows: The plaintiff was a manufacturer of prefabricated houses. He was in negotiations with the Ministry of Health who wanted to purchase a number of those houses. The plaintiff alleged that government officials represented to him that several of his houses were going to be purchased and that the necessary funds were or would be available for the transaction. In truth the Ministry was never able to purchase the said houses so that the negotiations fell through. The plaintiff sued the Ministry on the ground that he had incurred expenses and forgone other work in reasonable reliance on its negligent misrepresentation about the availability of funds.

1. The judgement

Lewis J. rejected the claim. The judge first referred to the two important cases of *Herschel v. Mrupe*[163] for the South African law and *Hedley Byrne v. Heller*[164] for the English law to set out the requirements for a successful claim in negligent misrepresentation. These are the 'knowledge, or its equivalent, that the information is desired for a serious purpose; that he to whom it is given intends to rely and act upon it; that, if false or erroneous, he will because of it be injured in person or property'. Also, the plaintiff must in morals and good conscience have the right to rely upon the information and the defendant must have a duty to give it with care.[165] Lewis J. found a further limitation in van den Heever J.A.'s submission that one expects the representee himself to use ordinary care and prudence in avoiding injury to himself.[166] Furthermore, Lewis J. invoked a statement of Lord Denning to limit liability to cases where the information is given in response to an enquiry for the guidance of the very person in the very transaction in question.[167]

After having thus stated what the limits of an action for negligent misrepresentation are, the judge went on to show, how in his opinion the present case was not covered by the scope of that action. First, he generally promulgated that during the course of negotiations each party is free to withdraw and has to bear its own risk of losing expenses that it incurred in anticipation of the contract. To back his argument he relied on the standard of an ordinary prudent seller who is

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[162] 1970 (1) SA 133.
[163] 1954 (3) SA 464.
[164] (1963) 2 All ER 575.
[165] *Herschel v. Mrupe* 1954 (3) SA 464 at 480.
[166] *Herschel v. Mrupe* 1954 (3) SA 464, at 488, 491.

deemed to know that there are a number of reasons for the failure of the negotiations.[168] Accordingly, he stated that the plaintiff had no right to rely upon the representation that money for the contract would be available. To allow that would mean that he could gamble on the fact that a contract might eventuate and retrieve his losses if no contract eventuates, although, he doesn't use the ordinary care and diligence in safeguarding his own interest by avoiding losses in the unsecured phase of precontractual dealings.[169]

Secondly, he mentioned that the plaintiff had not specifically inquired with regard to the sufficiency of funds. Hence, the Ministry couldn't know that he was attaching particular importance to this aspect and was relying on their representations.[170] Consequently, the limitations to an action of negligent misrepresentation as set out above, were not met.

As a last argument Lewis J. invoked the public and authoritarian character of the Government. As the government must always be free to allocate and expend the public funds according to the public interest, a private contractual partner has not the right to rely on any representation or promise to the effect that public funds would be available for their contract.[171]

2. Consideration

The judge addressed the specific problems of precontractual dealings but used them to reject outright any obligations that might occur because of the conduct of one of the parties in that phase. He was obviously of the opinion that by contrast to *Hedley Byrne* v. *Heller* the plaintiff in the present case had no right to rely on the representation, because it was made before a binding contract was concluded. It would have been more convincing if Lewis J. would have pointed out the differences of the cases more clearly. To denote the risk taking of the plaintiff as 'gambling' doesn't distinguish the case from *Hedley Byrne* v. *Heller*. There the plaintiff had also - relying on the misrepresentation - assessed the risk as minimal and, therefore, entered into the agreement, and furthermore, there was also no contract between Hedley Byrne and Heller. The cases of

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[167] *Candler* (1951) 1 All ER 426, at 435; *Murray v. McLean* 1970 (1) SA 133, at 137.

[168] At 137 - 8.

[169] At 138 - 9. Lewis J. also relied on *Hamman v. Moolman* 1968 (4) SA 340, where a negligent misrepresentation had induced a contract. It was held that there was no delictual claim because the plaintiff had to safeguard himself against losses by the precaution of requiring the representor to guarantee the truth of his representation. For the present case Lewis J. concluded that the plaintiff should have concluded a separate contract of indemnity with the defendant, at 139.

[170] Lewis J. invoked the decision of *Currie Motors (Pretoria) (Pty.) Ltd. v. Motor Union Insurance Co. Ltd.* 1961 (3) SA 872, at 876.

misrepresentation always deal with an estimation of risk which is made according to the misrepresentation.[172] Adjudication in other jurisdiction also shows that one cannot simply regard reliance upon a misrepresentation as unreasonable just because it was done precontractually, but that there are situations where a precontractual misrepresentation will lead to the liability of the representor.[173]

Furthermore, Lewis J. didn't apply the test as he had made it out in *Hedley Byrne* v. *Heller* and *Herschel* v. *Mrupe*. There, the second requirement for a viable claim for negligent misrepresentation is that 'the defendant *ought to* have known that the plaintiff was relying on him'[174], respectively, that the defendant must have had 'knowledge *or its equivalent*' about the reliance of the plaintiff on the representation[175]. In his reasoning, however, the judge limited this requirement to the mere knowledge of the plaintiff's reliance, which the defendant obtains through the inquiry of the plaintiff for the representation in question. He concluded, that the Ministry could not know that the plaintiff attached specific importance to the availability of funds, because he had not expressly enquired about that. The statement of facts says that the officers knew that the plaintiff was spending time and energy in preparing for the contract, that he was purchasing material for it, that he was foregoing other work and that he was incurring expenses which would be wasted unless the Ministry purchased the said houses.[176] In this context it seems quite reasonable to infer that the officers for the Ministry could and should have known that the plaintiff relied on their representation that money would be available for the project. This was obviously the major risk that the plaintiff was ready to accept following to the representation, and subsequently, incurred the before-mentioned expenses. Hence, Lewis J. could as well have argued

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[171] (1970) 1 SA 133, at 141.

[172] WHB Dean, Put Not Your Trust in Princes, Nor in the Son of Man, in Whom There is no Help - Psalm 146, Verse 3, *SALJ* 87 (1970) 149, at 152.

[173] *Markov* v. *ABC Transfer & Storage Co.* 76 Wash, 2d 388 (an American case); *Box* v. *Midland Bank Ltd.* (1979) 2 Lloyd's Rep. 391 (an English case); See also the cases of precontractual misrepresentation that induce a contract: P. M. A. Hunt, Damages for Negligent Misrepresentation Inducing Contract, *SALJ* 81 (1964), 241, at 244; P.M.A. Hunt, No Damages for Negligent Misrepresentation Inducing Contract? *SALJ* 85 (1968), 379, at 380; J. F. Coaker & W.P. Schutz, *Wille and Millin's Mercantile Law of South Africa*, 16th ed. (1967), at 76; although in *Hamman* v. *Moolman* 1968 (4) SA 340, at 347 - 8 Wessels J.A. denied in his obiter dictum that there can be liability for negligent misrepresentation inducing a contract; see also R. G. McKerron, Liability for Negligent Statements: *Hedley Byrne* v. *Heller*, *SALJ* 80 (1963), 483, at 488 - 9.

[174] *Hedley Byrne* v. *Heller* (1963) 2 All ER 575, at 583, 594, 601, 617.

[175] *Herschel* v. *Mrupe* 1954 (3) SA 464 at 480.

[176] *Murray* v. *McLean N. O.*, 1970 (1) SA 133, at 134 - 5.

that the defendant *ought to have known* that the plaintiff relied on the representation that funds were available.

The last criticism that one could raise about Lewis J.'s decision is his undifferentiated view of all cases of precontractual dealings. He equates his example of a shoeseller - who foregoes other business, because he fruitlessly serves a client - with the present case where two business persons negotiated for several months and both confidently anticipated that a contract would be concluded. This context should have some effect on the analysis whether it is reasonable to rely on the representation of the defendant or not.[177] Why should it be true that every reasonable man would insist to conclude a separate agreement about the expenses or that he refuses to incur expenses until a contract is concluded? In lengthy negotiations for an expensive contract the parties will often incur expenses, sometimes on their own risk, but sometimes also because of the conduct of the other party.[178] If this conduct constitutes a negligent misrepresentation in a business relationship, it is this misrepresentation that is reproachable and not the reliance of the other partner. It seems, accordingly, that his reliance is reasonable, at least more reasonable than the misrepresentation.

3. Conclusion

The judgement in *Murray* v. *McLean N.O.* should be reconsidered from a modern point of view, because the law of negligent misrepresentation has been developing since then. Also, other jurisdictions show, that there are cases of precontractual losses that deserve protection. Hence, one cannot say any longer, that simply because a representation is made precontractually it is unreasonable to rely on it and to act in reliance on it.

In the following, we need to discern under which circumstances a precontractual negligent misrepresentation can lead to the liability of the representor.

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[177] WHB Dean, *supra* n. 172, at 154.

[178] All the cases that were dealt with under restitution show that parties incur expenses in the precontractual phase because of the conduct (sometimes the request) of the negotiating partner: *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409 (request of the defendants); *Watson* v. *Watson,* (1953) NZLR 266 (encouragement of the defendant to render services); *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.* (1954) 1 Q.B. 428 (request); *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712 (request); *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880 (request).

II. Negligent misrepresentation in modern South African law

Misrepresentation is an incorrect or misleading statement of fact made by one party to the other before or at the time of the contract.[179] It may be made expressly, or impliedly, by conduct and even by silence if the representor has a duty to speak.[180] As opposed to intentional misrepresentation the negligent misrepresentation was recognised as a viable cause of action only some decades ago in *Administrateur Natal* v. *Trust Bank van Afrika Bpk.*[181]

In order to establish a case of negligent misrepresentation following requirements must be fulfilled: First, there must be an act, in these cases, a misrepresentation. This misrepresentation must, secondly, be wrongful, thirdly, negligent, and must fourthly have caused patrimonial loss to the plaintiff.[182] Precontractual misrepresentations mostly generate pure economic losses and the present thesis also limits its scope to cases of merely economic losses.

If and when the failure of negotiations can lead to the liability of a negotiating party under the law of negligent misrepresentation depends on the successful application of the above-mentioned requirements onto the cases in question.

1. Misrepresentation

First of all, precontractual liability for negligent misrepresentation can only encompass cases where one party utters an incorrect or misleading statement.

One could generalise and regard as the precontractual misrepresentation always the representation of the defendant that he has the will and ability to contract, which turns out to be incorrect since no contract eventuated.[183]

Misrepresentations must relate to a matter of ascertainable past or present fact.[184] Consequently, the mere opinion of one party about whether a contract will come about or not does not per se constitute a misrepresentation, neither does such a prediction. However, his intent to conclude a

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[179] D Hutchinson / R Zimmermann, Fahrlässige irreführende Angaben im vorvertraglichen Bereich, *ZEuP* 3 (1995) 271, at 277.

[180] D. Hutchinson / B. van Heerden / D. P. Visser / C.G van der Merwe, *Willes's Principles of South African Law* (1991), at 440; J. Neethling / J. M. Potgieter / P. J. Visser, *Law of Delict* (2nd ed.), at 286.

[181] (1979) 3 SA 824, at 832 - 33.

[182] J. Neethling et al., *supra* n. 180, at 287 - 293.

[183] D. Hutchinson, Damages for Negligent Misstatements Made in a Contractual Context, *SALJ* 98 (1981), 486, at 498; one could say that implicit in the act of negotiating is the serious intent to contract: E. A. Farnsworth, *supra* n. 4, at 234.

[184] *Feinstein* v. *Niggli* 1981 (2) SA 684, at 695; D. Hutchinson et al., *Wille's Principles*, *supra* n. 180, at 440.

contract shows the speaker's state of mind, which is a matter of fact[185] as much as the ability to contract is one, too. Accordingly, the representor's false statement about his willingness and ability to contract qualifies as a precontractual misrepresentation.

It is another issue, whether there are more and other precontractual statements which can entail liability. In *Murray* v. *McLean N.O.* for example, the plaintiff complained about the defendant's misstatement that he had sufficient funds to fulfil the anticipated contract. This concerns the defendant's ability to fulfil the contractual obligation (not his ability to contract). But certainly, the statement that enough funds are available for the contract promotes the plaintiff's understanding that the defendant also wants to conclude the contract. Also, when the defendant encourages or even asks the plaintiff to render services precontractually, this will in most cases show that the defendant wants to enter into the anticipated contract. Hence, every conduct of the defendant that encourages the plaintiff to incur expenses or forego other business precontractually will embody the representation that the defendant has the 'will and ability to contract'.

Nevertheless, the representation will often be true at the moment it is done, i.e. when both parties truly trust that a contract will be concluded.[186] Strictly spoken, the expenses that the plaintiff incurs are then not actionable as a tort of negligent misrepresentation (there is no *mis*representation, hence, no tort). The conduct of the defendant can, however, become a misrepresentation later, namely when it begins to be obvious for the defendant that he looses his will or ability to contract. Also, it can validly be argued that when an envisaged contract later fails, the defendant had misrepresented his **persisting** will and ability to contract. As the contract eventually doesn't come about, because of a change of attitude of the defendant, it is obvious that he must have misled the plaintiff in his belief that the defendant's attitude was meant to persist until the conclusion of the contract.[187]

The misrepresentation that the defendant has the will and ability to contract should, accordingly, be the general and minimum first requirement for a defendant's precontractual liability.

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[185] D. K. Allen, *Misrepresentation* (1988), at 12 - 13.

[186] See *Sabemo Pty Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880, at 902; *Regalian Properties plc.* v. *London Dockland Development Corp.* (1995) 1 All ER 1005, at 1009, where it was a common expectation that the contract would come about.

[187] In *Kern Trust (Edms) Bpk* v. *Hurter* Friedman J stated that also an opinion or forecast for a contract that is made precontractually can lead to liability, even if the speaker honestly believes in their correctness. He can be held liable for negligence, if he expressed the opinion without taking such steps as a reasonable person would take in the circumstances, to satisfy himself that such opinion or forecast was justified, 1981 (3) SA 607, at 618.

2. Wrongfulness

Since *Minister van Polisie* v. *Ewels* it is acknowledged, that in South African law, for liability to follow the damage must be caused in a wrongful, that is in a legally reprehensible or unreasonable manner.[188] Wrongfulness is given when the legal convictions of the community condemn the conduct in question and demand that the loss should be made good by the culprit.[189] It is a requirement that encompasses considerations of policy.[190] It is determined according to the criteria of reasonableness and - sometimes also - of objective foreseeability.[191]

In a case of physical harm a conduct will prima facie be wrongful. Not so if the defendant caused purely financial loss. Such economic loss is, indeed, since *Administrateur, Natal v. Trust Bank van Afrika Bpk* recognised as recoverable damage. But already then did judge Rumpff forward 'wrongfulness' as a device to control the scope of delictual claims and to avoid indeterminate liability.[192] Hence, the wrongfulness must be specifically established in each case of purely financial loss, i.e. also when the precontractual losses are purely economical.[193]

Furthermore, the law recognises that 'words are more volatile than deeds'.[194] Thus, where the defendant's conduct is in the nature of a verbal statement the wrongfulness must also be specifically established. As a result, in the cases that are presently scrutinised - cases of statements that cause pure economic loss - policy considerations for both the conduct and the loss need to be evaluated.

Hence, a negligent misrepresentation is wrongful, if the defendant was under a legal duty to furnish the correct information in the particular circumstances (conduct) and if he didn't fulfil that duty so that an intolerable financial loss occurred (loss).

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[188] D Hutchinson, *Aquilian Liability II (Twentieth Century)*, in: R. Zimmermann & D. Visser, *Southern Cross, Civil Law and Common Law in South Africa* (1996), at 624.

[189] Minister van Polisie v. Ewels, 1975 (3) 590, at 597; A van Aswegen, *Policy considerations in the law of delict*, THRHR (56) 1993, at 190.

[190] A van Aswegen, *supra* n. 189, at 171, 188.

[191] *Lillicrap, Wassenaar & Partners* v. *Pilkington Bros. (SA) (Pty.) Ltd.* 1985 1 SA 475, at 498; *Tsimatakopoulos* v. *Hemingway, Isaacs and Coetzee CC* 1993 4 SA 428; *Knop* v. *Johannesburg City Council* 1995 2 SA 1, at 27; J. R. Midgley, *Delict*, in: W. A. Joubert (ed.), *LAWSA* vol. 8 Part 1, at 50 - 51.

[192] See *Knop* v. *Johannesburg City Council* 1995 (2) SA 1, at 27 as a modern example of how this device is applied, D Hutchinson, *supra* n. 188, at 631.

[193] D Hutchinson & R Zimmermann, *supra* n. 179, at 284.

[194] *Hedley Byrne & Co. Ltd.* v. *Heller & Partners Ltd.* (1963) 2 All ER 575, at 613; J. R. Midgley, *supra* n. 191, at 48.

a) Wrongfulness of the conduct

Whether the defendant has a legal duty to give the correct information is to be determined by weighing the individual interests at stake in the light of the public interest and the circumstances.[195] Regarding the case of *Murray* v. *McLean N.O.*, the individual interests in cases of precontractual liability are the following: the plaintiff's interest to be able to rely on a representation that induces him to incur expenses and the defendant's freedom to act uninhibitedly during the precontractual phase, where he is not yet contractually bound.[196]

The primary public concern against any precontractual liability is its newness. As Grosskopf AJA stated in *Lillicrap, Wassenaar & Partners* v. *Pilkington Brothers*, the South African law adopts a conservative approach to the extension of remedies under the *lex Aquilia*.[197] Hence, the extension of delictual liability for negligent misrepresentation into the precontractual sphere has to be justified by convincing arguments. Generally, precontractual representations that are vague and non-factual puffs, e.g. loose, exaggerated statements in praise of wares, are not actionable.[198] By contrast, the Appellate Division in *Bayer SA (Pty.) Ltd.* v. *Frost* has acknowledged liability for a precontractual misrepresentation that is made to induce the other party to contract.[199] Hence, precontractual misrepresentations are not by itself excluded from liability for negligent misstatements and we can analyse whether cases can be wrongful where not the conclusion of a contract was induced, but merely precontractual expenses.

Adjudication concerning misstatements sensed that, in particular, following factors are relevant to balance the different interests and determine whether a misstatement is wrongful: The nature of the harm; the nature of the statement and the context in which it is made; the truth of the statement; the purpose of such statement and the defendant's knowledge of such purpose; the relationship

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[195] *Knop* v. *Johannesburg City Council* 1995 2 SA 1, at 28; J. R. Midgley, *supra* n. 191, at 50, 59; J. Neethling et al., *supra* n. 180, at 288.

[196] An interest that he promotes by his presentations, J. Neethling et al. *supra* n. 180, at 32.

[197] (1985) 1 SA 475, at 500; *Administrateur Natal* v. *Trust Bank van Afrika Bpk* (1979) 3 SA 824, at 831, 832-33; *Hamman* v. *Moolman* (1968) 4 SA 340, at 348.

[198] D. Hutchinson et al., *Wille's Principles, supra* n. 180, at 441; D. K.Allen, *supra* n. 185, at 14.

[199] Against: *Hamman* v. *Moolman* 1968 (4) SA 340; in favour of liability: *Kern Trust (Edms.) Bpk* v. *Hurter* 1981 (3) SA 607, but this case was decided by a Provincial Division; only in *Bayer South Africa (Pty.) Ltd.* v. *Frost* 1991 (4) SA 559 did the Appellate Division unequivocally recognise that there is a delictual claim for damages when a negligent misrepresentation induces the representee to contract; J.T.R. Gibson, *South African Mercantile and Company Law* (7. ed. 1997), at 73; D. Hutchinson et al., *Wille's Principles, supra* n. 180, at 441. See for the same attitude in English law for negligent misstatements made precontractually: R. F. V. Heuston, R. A. Buckley, *Salmond and Heuston on the law of torts* (1992), at 217.

between the parties, for example whether professional or contractual; whether the statement was made in a professional capacity; whether the plaintiff could reasonably rely on the defendant's knowledge and skill or the information conveyed; the severity and extent of the harm; whether the harm was foreseeable; whether the defendant took any reasonable precautions to ensure the accuracy of the statement; whether any general considerations of public policy and fairness would favour the denial of a remedy.[200]

These factors must now be applied to cases of precontractual representations inducing expenses.

(1) Extent, severity of the harm - generally

The subsequent chapter, that considers whether the harm is wrongful, will scrutinise the nature, extent, severity and foreseeability of the harm. For now it suffices to state that the expenses that one party incurs precontractually can be vast. For example the English cases that have been analysed previously, showed that a plaintiff can spend months and even years to prepare a contract.[201] Then he spends working time, makes expenses and often foregoes other business which results in an economic loss that the plaintiff will never be rewarded for, if the defendant breaks off the negotiations. Therefore, the loss that a plaintiff can suffer from precontractual expenses is considerable, which suggests that a remedy is justified in case the defendant causes such damage by his wrongful conduct.

(2) Nature and context of the statement – reasonable reliance

The **nature of the statement** and the context in which it is made is the first and, probably, the most important indication for, respectively against, its wrongfulness. The nature of a precontractual misrepresentation is not one of pure facts, but rather one that reflects the defendant's will to contract or which prospects - according to him - the envisaged contract has. Such representations of 'internal' factors are far more uncertain than a statement of perceptible facts. Hence, it is less reasonable for a plaintiff to rely on such a representation. On the other hand, liability for the misrepresentation of such 'internal' factors always requires that the defendant showed an ascertainable conduct which is then as perceptible as a mere fact. Furthermore, when

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[200] *International Shipping Co. (Pty) Ltd.* v. *Bentley* 1990 (1) SA 680, at 694; *Standard Chartered Bank of Canada* v. *Nedperm Bank Ltd.* 1994 (4) SA 747, at, 770; J. R. Midgley, *supra* n. 191, at 69.

[201] *William Lacey (Hounslow)* v. *Davis* (1957) 2 All ER 712; *Sabemo Pty Ltd.* v. *North Sydney Municipal Council* (1977) 2 NSWLR 880 ($ 300,000); *Regalian Properties plc.* v. *London Dockland Development Corp.* (1995) 1 All ER 1005 (3 m Pounds).

the defendant represents his ability to contract, the representation is one of objective fact in the first place.

The **context** of such a statement is precontractual, which is the core problem of these cases. On the one side the freedom of contract, which allows each party to choose not to contract, favours the defendant's viewpoint.[202] On the other side, this principle does not allow him to harm his negotiating partner. Liability for a misrepresentation would not force the defendant to contract, but to pay for damages that he caused by his negligent conduct. Still, the precontractual phase is one of risk for both partners, because both know, that a contract is not yet concluded and neither has a guarantee for performance.[203]

The consideration of plaintiff's **reasonable reliance** on the defendant's conduct might tip the balance.[204] Even though, the negotiating partners act in a sphere of risk, it happens regularly, that the parties seriously anticipate a contract and that the defendant actively excludes the plaintiff's risk - of not getting the contract - by his conduct. In such cases it might be reasonable for the plaintiff to rely on the representation and to incur expenses.[205]

The difficulty consists in determining, when the defendant's conduct is such that the plaintiff could reasonably regard his risk as excluded. In order to draw a hard and fast line one could deny that it can never be reasonable to rely on a negligent - as opposed to an intentional[206] - precontractual misrepresentation, as Lewis J. did in *Murray* v. *McLean N.O.* The recipient of a statement, though, will not be able to distinguish if the defendant makes a false or a true representation and neither whether the misrepresentation is intentional or negligent. Consequently, one cannot regard the reliance of the plaintiff in the one case as reasonable and in the other case as unreasonable. We

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[202] The exercise of a right can be the defence to a tort action, but may - as a competing interest - in first place operate as determinant for or against the unlawfulness of the defendant's conduct (depending on its scope), J. R. Midgley, *supra* n. 191, at 93.

[203] See *William Lacey (Hounslow) Ltd.* v. *Davis* (1957) 2 All ER 712, at 714, E. A. Farnsworth, *supra* n. 4, at 221.

[204] For liability for a misstatement the reasonable reliance is essential: 'If a man makes a statement in regard to a matter upon which his hearer may reasonably suppose he has the means of information, and that he is speaking with full knowledge, and the statement is made as part of a business transaction, or to induce action from which the speaker expects to gain an advantage, he should be held liable for the consequences of reliance upon his misstatement.', Williston on Contracts as cited in: D Hutchinson, *supra* n. 183, at 491. Such evaluation can logically also apply to the representation of the speakers will and ability to contract, where the hearer must suppose that his vis-à-vis speaks in knowledge about his will and ability or even opinion about the forecast of the contract. This was recognised in *Kern Trust (Edms) Bpk* v. *Hurter* 1981 (3) SA 607, at 618 A-D. In English law the term of reliance on a statement was introduced in *Hedley Byrne & Co. Ltd.* v. *Heller and Partners Ltd.* (1963) 2 All ER 575, at 583, 591 to limit liability for misstatements.

[205] WHB Dean, *supra* n. 172, at 152 - 153.

[206] It is uncontested that a defendant is liable for an intentional misrepresentation.

can only concentrate on the external conduct of the defendant and how a reasonable person must have understood and reacted to that conduct.[207]

There are indicators demonstrating that a reasonable person is nowadays allowed to rely on a precontractual representation, when it shows the defendant's serious will and ability to conclude a certain contract.

First, the **relationship of the parties** is relatively close, certainly closer than the relationship of mere strangers. Especially after lengthy negotiations, assurances of the seriousness with which the contract is anticipated, or the demand of the defendant that the plaintiff starts preparing for the contract, can the plaintiff reasonably expect a fair and diligent handling of the mutual expectancies. This is confirmed by and due to the fact that South African law contains a principle of good faith.[208] Recent adjudication has esteemed that parties owe each other fair dealings to some extent also precontractually.[209] Hence, the parties' relationship is such, that they can reasonably rely on each other's representations with regard to the anticipated mutual performances.

Secondly, the practice of business persons suggests that negotiating partners rely on each other already before the conclusion of a contract. The number of only Anglo-American cases shows already how frequently negotiating parties run the risk of making expenses precontractually in the course of mutual contemplation about the execution of the contract.[210] It is nowadays customary that negotiations are often long, so that they constitute a gradual process, and businessmen have to co-operate and if necessary, make expenses to prepare for the deal.[211] They wouldn't spend any money or effort if they wouldn't rely on their vis-à-vis' representation that a contract is seriously anticipated.

Consequently, it is in principle reasonable to rely on the defendant's precontractual representation that he bears the will and ability to contract.

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[207] C Lewis, Damages for Negligent Misrepresentation - The Appellate Division Leaps Forward, *SALJ* 109 (1992) 381, at 384.

[208] PMA Hunt, *SALJ* 1968, *supra* n. 173, at 380; D Hutchinson, *Good Faith in the South African Law of Contract*, in: R Brownsword / NJ Hird / G Howells, *Good Faith in Contract: Concept and Contract*, at 241 f.

[209] *Bayer SA (Pty.) Ltd.* v. *Frost*, (1991) 4 SA 559, at 568, 575; considering: D Hutchinson, *supra* n. 208, at 241 f.

[210] *Jennings and Chapman Ltd.* v. *Woodman Matthews & Co.* (1952) 2 TLR 409; *Brewer Street Investments Ltd.* v. *Barclays Woollen Co. Ltd.*, (1954) 1 Q.B. 428; *William Lacey (Hounslow) Ltd.* v. *Davis*, (1957) 2 All ER 712; *Regalian Properties plc* v. *London Dockland Development Corp.* (1995) 1, 1005; *Sabemo Pty. Ltd.* v. *North Sydney Municipal Council*, (1977) 2 NSWLR, 880; *Brenner and Another* v. *First Artists' Management Pty. Ltd. and Another*, V. R. (1993) 2, 221.

[211] E. A. Farnsworth, *supra* n. 4, at 219 f.

(3) Knowledge or its equivalent of the plaintiff's reliance

Mere reliance does not suffice, however, because in order to be a wrongful representation the defendant must have been able to realise that the plaintiff will rely on his representation.[212]
It will have to be inferred from the circumstances of the case, whether the conduct of both parties was such that the defendant had to understand that the plaintiff would act on his misrepresentation. One might generally maintain that the stronger the representation of the defendant is and the more it reassures the plaintiff about the prospects of the contract and encourages him to start preparing for it, the more the defendant will be considered to have known that the plaintiff relied on his representation. Certainly, also the plaintiff's conduct during negotiations plays a crucial role. When he doesn't indicated at all that he believes in the defendants will and ability to contract or that he will surely wait until a contract is finally signed, the defendant can not foresee that the plaintiff will make precontractual expenses trusting on his representation.
Thus, according to the circumstances the defendant will know about plaintiff's reliance. Since there can in principle be knowledge or its equivalent of the reliance, a misrepresentation despite reliance and that knowledge will be wrongful.

(4) Conclusion

It is wrongful to precontractually misrepresent the will and ability to conclude the envisaged contract.
One has to keep in mind, however, that there are several reasons for negotiations to fail - the parties eventually don't agree on the terms, technical difficulties inhibit the performance of the envisaged contract etc. Only if the defendant deceives the plaintiff's trust into his will and ability to contract, e.g. when he withdraws from the negotiations out of pure whimsy, can the plaintiff expect compensation.
Considerations of policy play the final role to determine, whether precontractual misrepresentations can be wrongful.[213] Such policy considerations will adequately be dealt with later as they concern the problem of precontractual liability as a whole, not merely the wrongfulness of the conduct.

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[212] *Standard Chartered Bank of Canada* v. *Nedperm Bank Ltd.* 1994 (4) SA 747, at 770; WHB Dean, *supra* n. 172, at 153; McKerron, *supra* n. 173, at 488.
[213] J. R. Midgley, *supra* n. 191, at 59.

Hence, so far more arguments point to the wrongfulness of a precontractual misrepresentation than against it.

b) Wrongfulness of the harm

The economic loss that negligent misstatements can generate has to be wrongful in order to be recompensed. A conduct that leads to economic loss is only regarded as wrongful if a value judgement in the light of policy considerations commands that the defendant should be vested with liability.[214]

The considerations that operate for such a judgement are: whether the conduct is sanctioned by law; whether the loss is finite; whether the number of potential plaintiffs is limited and identifiable; the foreseeability of the harm and the likelihood of it occurring;[215] the availability of protective measures, and to whom they are available; any special skills and responsibilities; the ease with which the measures could have been implemented, their cost, and the likelihood of their success; the parties' respective interests; the relationship of the parties to one another; whether there will be further consequential liability; the social consequences of imposing liability; the need for legal certainty; the extent of the duty which would be placed on others in a similar position to the defendant; the need for a delictual remedy; and finally, whether there are any considerations of equity, fairness and policy which favour the denial of a remedy.[216]

Again, the characteristics of precontractual misrepresentations, that cause economic loss, must be considered by means of these points of reference - as far as they are sensibly applicable.[217]

(1) Scope of loss and liability

The **loss** is finite, the number of the potential plaintiffs is limited and identifiable and there will be no further consequential liability. The claimant can only be the negotiating partner and the loss he could claim is limited to his precontractual expenses and maybe the lost profit of business

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[214] D Hutchinson, *Aquilian Liability II, supra* n. 188, at 631, J. R. Midgley, *supra* n. 191, at 59 and 72.

[215] See also *Government of the Republic of South Africa* v. *Basdeo and Another*, 1996 (1) SA 355, at 368 f.

[216] J. R. Midgley, *supra* n. 191, at 72.

[217] Some of the elements have already been sufficiently dealt with under the wrongfulness of the conduct such as the relationship of the parties and their respective interests. As far as they don't give rise to further consideration they will not be evaluated again.

opportunities that he has foregone. With the claim of the plaintiff the case will be closed.[218] Hence, there is no danger of indeterminate liability, which points strongly to the wrongfulness of such economic loss.

(2) Foreseeability, likelihood and extent of the harm

The **foreseeability of the harm and its extent** is a factor which is not bringing the complicated issue much further.

On the one side, a harm is foreseeable, when the defendant represents his will and ability to contract in a way that a reasonable plaintiff will rely on it, and will consequently make expenditures trusting in this representation.

On the other side, one could expect the plaintiff to protect himself by either not making precontractual expenses at all or by insisting on a separate agreement about those costs.[219]

It will depend on the circumstances, whether the defendant could foresee precontractual costs. The parties might or might not have spoken about precontractual preparatory works, or sometimes, the defendant will even expect the plaintiff to incur such costs.[220]

Furthermore, the harm is foreseeable when there is some probability of the negotiations to fail that the defendant knows about. If he knows or can reasonably foresee that he might loose his will or ability to contract, he also foresees that the plaintiff then incurs his precontractual costs in vain.

Certainly, there can be an equal contributory negligence of the plaintiff who could just as well have foreseen the prospects of the contract and have prevented his harm. The likelihood with which the harm will occur depends on these very same circumstances.

(3) Availability of protective measures

The availability of **protective measures**, to whom they are available, their costs, the likelihood of their success and how easily they could have been implemented oppose the wrongfulness of the harm.

As just mentioned, the plaintiff could have prevented his harm by simply insisting on the sharing of precontractual costs, or by refusing to incur those costs. [221] It would not be an expensive measure,

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[218] Any subcontractor that might suffer a loss, because he was instructed by the plaintiff – see *Regalian* – to prepare for the same contract, will not have relied on the misrepresentation of the defendant. He will also have a direct relationship to the plaintiff so that any liability for losses of subcontractors is impossible.

[219] See the obiter of Wessels J.A. cited in *Bayer* v. *Frost* (1991) 4 SA 559, at 567.

[220] See for example the English and Australian cases mentioned in note 188.

it is easily available to the plaintiff and most likely to spare him the disappointment of making unrewarded, futile expenses.

The only counter-argument is, again, the practice of business people that contradicts such conduct.[222] Often it is not convenient to show doubts about the prospects of the contract. The party who insists on a separate agreement about precontractual costs or refuses to incur them, runs the risk that his partner will be put off by this expectation. In case, that the partner is economically superior and can choose amongst many other competitors, the exigent one can even loose the chance to win the contract at all. [223] Also, some writers regard the argument that the plaintiff should have safeguarded his own interests as a light argument, because the South African law of contract is based on the principle of good faith and *caveat venditor*.[224] But in the precontractual sphere the good faith argument is less convincing. The defendant doesn't make a statement with regard to the content of his contractual performance - for which the protection of the plaintiff's good faith fully applies - but merely with regard to the prospects of concluding a contract. This still leaves the plaintiff with the uncertainty whether all other conditions will be fulfilled to bring about a contract.

Consequently, the argument stays that the plaintiff can easily safeguard himself against precontractual costs.

(4) Special responsibility of the defendant

There are no special skills of the defendant that the plaintiff could rely on. But each party is **responsible** to reassure itself about the hindrances to the future contract. Hence, it is within the responsibility of the defendant to undeceive the plaintiff about perceivable impediments to the contract. If he doesn't do so, the harm caused by the defendant's omission is wrongfully caused.

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[221] *Hamman* v. *Moolman,* 1968 (4) SA 340, at 348; *Murray* v. *McLean, N.O.*, 1970 (1) SA 133, at 138 - 139; PQR Boberg, The Protection of Interests of Substance: The Aquilian Action *1970 Ann. Survey* 159 - 160; WHB Dean, *supra* n. 172, at 154 - 155; R. McKerron, *supra* n. 173, at 489.

[222] WHB Dean, *supra* n. 172, at 155; D Hutchinson & R Zimmermann, *supra* n. 179, at 281.

[223] This is mostly the case for sub-supplier in the automobile industry. On the other hand, when a small sub-supplier doesn't insist on the immediate payment of precontractual expenses he will also not claim these costs under precontractual liability in case the contract fails to be concluded. He will rather bear those costs without complaining in order to get another chance later.

[224] PMA Hunt, *SALJ* 1963, *supra* n. 173, at 383; similar: D Hutchinson, *supra* n. 183, at 490 – 491 and 494.

(5) Social consequences of liability

The **social consequences** of imposing liability can be twofold. The parties might secure their interests by contracts about precontractual expenses in order to avoid the imposed delictual liability. Furthermore, they might be discouraged to freely negotiate which could have a detrimental effect on the economy.[225]

The first consequence would be positive, since it would create legal certainty about the sharing of precontractual costs and promote an in principle fair balance of the respective interests. The second consequence is negative, but not likely to occur. The legal systems – mainly European continental systems - that do protect precontractual reliance don't suffer from intimidated economies. For example, the Israeli law of contract has introduced the protection of good faith in precontractual dealings in 1973 and this further liability didn't produce negative effects on the Israeli economy.[226] Hence, the social consequences will rather be positive, which renders harm caused by precontractual misrepresentations wrongful.

(6) Legal certainty

The **legal certainty** will supposedly neither be increased nor diminished by imposing precontractual liability.

On the one hand it will be very difficult to limit liability to deserving cases, and therefore, to create legal certainty with regard to the extent of liability.[227] On the other hand, certainty can be created – as indicated above –by contractual agreements of the parties themselves, who know that liability impends if they don't care for an equitable balance of their precontractual costs.

Even though, it is legally objectionable to pass the burden of creating certainty on to the parties, the fact remains that they are the closest to their needs and can appropriately deal with their risks. Also, the case law proves that even now, where there is no explicitly recognised liability, parties might doubt whether they could nevertheless succeed with a claim in light of the development of the law of delict.[228] Therefore, the desire for legal certainty doesn't oppose precontractual liability.

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[225] This is the fear of English lawyers and was the fear of Israelien lawyers before Art. 12 of the Israelien contract law was introduced that provides for good faith also precontractually: A M Rabello, *supra* n. 4, at 59.

[226] A M Rabello, *supra* n. 4, at 40, 41, 59.

[227] See e.g. the previous considerations with regard to the foreseeability of harm which depends entirely on the circumstances and the reasonable reliance on a precontractual representation.

[228] See D Hutchinson, in: Brownsword (ed.), *supra* n. 208, at 242.

(7) Effects of granting liability and need for liability

The **extent of the duty that would be placed on others in a similar position to the defendant** speaks for liability. Only when the defendant committed a negligent misrepresentation that the plaintiff could reasonable rely on, will liability be imposed. It is not a high demand to expect negotiating partners to scrutinise one's own forecast and requirements for the envisaged contract and then not to make misrepresentations.

There is also a **need for a delictual remedy**. As *Murray* v. *McLean N.O.* showed, there is no other remedy available.[229] The law of contract does not – yet – provide for precontractual expenses.

(8) Conclusion

Most of the argument fight in favour of the wrongfulness of causing economic loss precontractually. Although, there are valid doubts against liability, the crucial element is the defendant's responsibility for a loss, which will in most cases of failed negotiations be foreseeable and which is limited to this specific case.

c) Considerations of policy

Finally, we have to ask whether any considerations of policy, fairness and equity speak for a denial of a delictual remedy for precontractual expenses.

There are hardly further doubts against precontractual liability than the ones already dealt with under the criteria that establish the wrongfulness of the conduct and the harm. As to the reasons of policy: they could concern the question whether there could be a detrimental effect on the economy, whether the legal certainty will be undermined, whether it is too far-reaching to allow a delictual claim having regard of the freedom of contract etc. All these deliberations have been addressed. The fairness of liability concerns the question whether it is fair for the defendant to have to pay for precontractual expenses. The answer is, yes, if he negligently induced the plaintiff to reasonably rely on his misrepresentation.

And there are no further reasons of equity against liability.

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[229] D Hutchinson, *supra* n. 183, at 492 for precontractual misstatement inducing a contract, then there is also no remedy when the contract fails.

d) Conclusion

As a result, a negligent misrepresentation is wrongful if the defendant made a reasonable plaintiff believe that a contract will come about and that he will be rewarded for his expenses.
There are many doubts and also valid reasons for the defendant's position – his freedom of contract, that the precontractual phase is one of risk for both parties and that the plaintiff could easily protect himself by insisting on a previous agreement about the costs.
However, liability is justified when the defendant shows such conduct as to make a reasonable person trust in his will and ability to contract. The inducement for the precontractual expenses is then coming from his sphere and it would be unfair to let the plaintiff sit on costs that are often immense. If both parties negotiate and prepare for a contract it cannot be right if only one of them has to bear all costs.[230]
Finally, the argument that also the plaintiff could have safeguarded his own interests and must know that he relies on a precontractual, thus, not a binding representation, will have to be considered as his contributory negligence. Then, these arguments can lead to a sharing of the costs, but they cannot preclude the judgement that the defendant acted wrongfully.

3. Negligence

A negligent misrepresentation is one made honestly but carelessly, that is, without the care that a reasonable person would have shown in the circumstances.[231] To find out how a reasonable person would have acted, one has to consider the matter objectively from the defendant's point of view by asking whether in his situation the harm to the plaintiff was reasonably foreseeable and preventable.[232]
The decision whether the defendant acted in such a careless way has to be taken in each case according to the circumstances and with having specific regard to the potential gravity and extent of the harm risked.[233] Generally, one can only say, that if two parties negotiate for a long time, if the defendant induces the plaintiff to start preparing for the contract or if he reassures him that a

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[230] Hunt, *SALJ* 1964, *supra* n. 173, at 244.
[231] D. Hutchinson et al., *Wille's Principles, supra* n. 180, at 443.
[232] J. Neethling et al., *supra* n. 180, at 290; J. R. Midgley, *supra* n. 191, at 52, 126, 131. For English law: R.F.V. Heuston, R. A. Buckley, *supra* n. 199, at 231 - 232.
[233] J. R. Midgley, *supra* n. 191, at 126, the fact that the loss is a purely financial one, doesn't reduce the foreseeability test.

contract will certainly be concluded, then it can be foreseeable that such a plaintiff will incur precontractual expenses. These expenses will constitute a harm if no contract eventuates.

The defendant must take such steps as a reasonable person would take in the circumstances to satisfy himself that his opinion or forecast for a future conclusion of a contract is justified.[234] If the defendant could have foreseen that there is a hindrance to the contract in his sphere or that he will retire from the negotiations, he will have acted negligently when he either actively represents his will and ability to contract or if he omits to warn the plaintiff against incurring those costs.

When negligence is established, one has to consider whether the prejudiced party is responsible for contributory negligence.[235] As it was mentioned above, the fact that the parties act in a sphere of risk, and therefore, each of them must be wary, can lead to contributory negligence. It will depend on the specific circumstances whether the plaintiff was justified in fully relying on the defendants representation. For example the force of the representation, the amount of the costs or the closeness of the parties relationship can then play a role.

4. Causation of patrimonial loss

The misrepresentation leads to liability when it caused a patrimonial loss to the plaintiff. This entails the causal link between the misrepresentation and the occurrence of a patrimonial loss.

Causation in South African law is divided into factual and legal causation.

First, the damage must have been factually caused. This can be tested according to the *conditio sine qua non* formula.[236] The misrepresentation must be a necessary condition for the plaintiff's misunderstanding, which in turn must be the reason for his damage, i.e. his incurring expenses. The causal link misses for example when the contract fails for a reason other than that to which the misrepresentation relates.[237] This will exclude undeserving cases, because it was another risk that materialised and not the one that the defendant excluded vis-à-vis the plaintiff by his misrepresentation.

Legal causation exists, when the nexus between the defendant's act and its consequence is sufficiently close to justify that the consequence is imputed to him.[238]

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[234] Compare: *Kern Trust(Edms) Bpk* v. *Hurter* 1981 (3) SA 607, at 618.

[235] J Neethling et al, *supra* n. 180, at 290.

[236] J Neethling et al. *supra* n. 180, at 291 suggests to follow another test, namely whether 'one fact arises out of another'. This way of questioning the causal link won't provide substantially different results.

[237] WHB Dean, *supra* n. 172, at 155.

[238] *Standard Chartered Bank of Canada* v. *Nedperm Bank Ltd.* 1994 (4) SA 747, at 764.

Policy considerations such as reasonableness, equity and justice have to be taken into account in order to uphold such a nexus. When the damage is an adequate and foreseeable – i.e. not too remote - result of the misrepresentation, it is caused in a legal sense.[239] The costs that the plaintiff incurred for the preparation of the contract will be adequately caused, if they are a direct result from his trust into the defendants misrepresentation. This will again depend on the circumstances of each case, but generally a reasonable plaintiff will only make expenses when he was reassured that they will not be in vain. Particularly expenses that enable and help him to fulfil his future obligation, will be a foreseeable damage.

Recoverable damages under the law of delict are all patrimonial losses. This includes monetary and pure economic loss.[240] Precontractual cases will mainly deal with preparatory expenses. Conceivable are costs for preparatory architectural or development plans and working schemes or even the beginning of the work itself. Losses that will not be included are lost profits of the deal itself, because they would give the plaintiff the benefit of the agreement that failed. This would be a typically contractual damage and is not justifiable in tort law, especially as the freedom not to contract forbids to hold the defendant practically bound by an agreement that he doesn't want to conclude.[241]

III. Conclusion

The South African law of negligent misrepresentation can be applied to cases of precontractual liability. This tort gives room to the considerations that suggest themselves when dealing with the balance of the two parties' interests in such a situation. As opposed to a claim under unjustified enrichment the law of delict offers the tool of contributory negligence to divide the wasted costs between the parties according to their responsibility for the causation of the damage. Furthermore,

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[239] *International Shipping Co. (Pty.) Ltd.* v. *Bentley* 1990 (1) SA 680, at 700. It should be noted that in this case the court dealt with the contributing conduct of the plaintiff under legal causation (at 698, 699, 701). A negligent conduct of the plaintiff himself that contributes to the damage is also causing the damage – either cumulatively or alternatively. As contributory negligence is an element of the claim of its own, it should also be dealt with as such. If the contributory negligence totally supersedes the defendant's conduct, the factual causal link might be interrupted, but when it simply contributes, one shouldn't analyse the weight of the contribution within the element of legal causation. J Neethling et al, *supra* n. 180, at 492.

[240] J. R. Midgley, *supra* n. 191, at 29.

[241] E. A. Farnsworth, *supra* n. 4, at 223. A later chapter will deal more specifically with the recoverable losses under all the possible remedies for damages resulting from failed negotiations.

it looks primarily at the conduct of the defendant as a reason for liability[242], which is neglected in the English law of restitution.

One factor that speaks against negligent misrepresentation as an appropriate remedy, is that it needs a misrepresentation to start with. The reason for the damages of the plaintiff is, however, not only that the defendant misrepresented his will and ability to contract. The reason for his loss is also that the defendant abandoned the contract. Then, it will often be difficult to argue, why his misrepresentation is so reproachable as to hold him liable, since, what we truly condemn is that he left the negotiations without good reason. It is true, that to name this veritable reason opens the claim even more to the criticism that the freedom not to contract is undermined. But to bring the claim under negligent misrepresentation complicates the issue even more and blurs why we want to grant liability despite the freedom of contract. It is true, that the tort of negligent misrepresentation offers the correct tools for arguing this claim - the plaintiff must have reasonably relied and the defendant must have been able to foresee his reliance and the harm. Accordingly, in South African law negligent misrepresentation will be the most appropriate basis for the plaintiff's demand to be recompensed for his precontractual expenses. As *Lillicrap, Wassenaar and Partners* v. *Pilkington Brothers* has shown, the South African law of delict will only slowly open itself to new grounds of liability.[243] It will be even more difficult to found a claim for precontractual losses on an even newer basis like the duty to act with good faith in precontractual dealings,[244] even though, such a basis will be more appropriate as it calls a spade a spade.

D. Culpa in contrahendo

Lastly, many civilian systems operate with a specific claim, the culpa in contrahendo, i.e. fault during negotiations.[245] This claim roots in good faith and has been developed for situations where

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[242] Liability is rather based on the improper conduct of the misrepresenting party: D Hutchinson, in: R Brownsword (ed.) *supra* n. 108, at 236, 242.

[243] (1985) 1 SA 475, at 500.

[244] Although, the concept of good faith in South African law is extended to the precontractual phase: *Savage and Lovemore Mining (Pty.) Ltd.* v. *International Shipping Co (Pty) Ltd.* (1987) 2 SA 149 at 198; D Hutchinson, in R Brownsword (ed.), *supra* n. 208, at 235.

[245] Art. 1337 Italian Civil Code; Art. 12 Israeli law of contracts (Israeli law has a common law basis, but codified many basics of its law, so that is it nowadays rather a mixture between the two systems.). A. M. Rabello, *supra* n. 4, at 51 f.; culpa in contrahendo in German law (a legal instrument that was established by legal analogy from norms that in specific cases oblige a person to pay damages for faulty precontractual conduct): Palandt-Heinrichs, *Bürgerliches Gesetzbuch*, § 276, digit 65.

lawyers considered the respective parties being close to each other, and therefore, more worthy of protection than mere strangers when their good faith is disappointed by a culpable conduct.[246]
Using the German culpa in contrahendo as an example I will now apply this remedy to cases of failed negotiations.

I. Basis of liability

Also German law regards the freedom of contract as a basic value, and thus, as a limitation for liability. The freedom of contract allows the defendant to abstain from contracting without having to give any reasons. Having knowledge about the fact that the plaintiff incurs expenses doesn't establish liability.[247] The borderline for the defendant's accountability is crossed when he negligently nourishes the plaintiff's legitimate trust, that the conclusion of the contract is certain, and when he then desists from it without good reason.[248]
The *culpa in contrahendo* (*cic*) is not a codified claim, but has been developed through legal analogy to several norms of the civil code. These norms do all bear the idea, that the defendant is accountable for certain harming acts that he undertakes during the preparation of the contract.[249]
Based on the purpose of these norms adjudication and legal doctrine deduced the rule that once a certain legally relevant contact exists between the parties, they owe each other the diligence of contractual parties.[250] Nowadays the *cic* is recognised as customary law.[251]
Since the special duties owed to each other do not exist towards the public in general, *cic* is not considered a mere extension of tortious liability. On the other hand, it is not regarded to be based on contract either, because the duties arise regardless of whether a contract comes about or not.[252]

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[246] R v. Jhering, *Culpa in contrahendo*, (1861) 51/52/53, 110/111/112.
[247] BGH NJW 1967, 2199; BGH WM 1972, 772; BGH NJW 1975, 43, 44; BGH WM 1977, 620; B. S. Markesinis, W. Lorenz, G. Dannemann, *The German Law of Obligations, Vol. I, The Law of Contract and Restitution, A Comparative Introduction* (1997), at 69; Palandt-Heinrichs, *supra* n. 245, § 276, digit 72.
[248] BGH BB 1955, 429; BGH MDR 1961, 49; BGH NJW 1967, 2199; BGH NJW 1975, 1774; BGH NJW-RR 1989, 627, 628; Staudinger-Löwisch, *Kommentar zum Bürgerlichen Gesetzbuch, Zweites Buch, §§ 255 - 292* (1995), preliminary remark to §§ 275 ff., digit 66; B. S. Markesinis, *supra* n. 247, at 69.
[249] H Brox, *Allgemeines Schuldrecht* (1992), digit 56. Such a norm is for example § 307 BGB: the debtor is liable when the contract is void because his performance of the contract was from the start subjectively impossible; § 122: reliance damage for rescission on the ground of mistake.
[250] Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 50 - 53, Palandt-Heinrichs, *supra* n. 245, § 276, digit 65; B. S. Markesinis, *supra* n. 247, at 64.
[251] Palandt-Heinrichs, *supra* n. 245, § 276, digit 65; Staudinger-Löwisch, *supra* n. 248, prelim. remark to §§ 275 ff., digit 39; Brox, *supra* n. 249, digit 56.
[252] B. S. Markesinis, *supra* n. 247, at 64.

Therefore, the *culpa in contrahendo* is mostly perceived as a third lane between contract and tort and often named a quasi-contractual basis of liability.

The *cic* has been applied to a diversity of different cases, of which many should belong to the law of delict, if the German tort law was not so inappropriate. As a result, there is a vivid discussion about the true reason for liability under *cic*.[253] Following grounds for liability are mostly forwarded: (1) The violation of the duty to protect the plaintiff's interest during negotiations.[254] (2) A newer and widely appreciated approach is the idea that the defendant offers and the plaintiff accepts special confidence during their precontractual dealings, which the defendant then disappoints – this corresponds with the protection of good faith.[255] (3) Another explanation is that there is a general professional liability for certain professionals such as lawyers and tax consultants, because the public recognises and trusts in their services while depending on them.[256]

As the *cic* is so widely applicable we should look at the liability's foundation in the context of the here relevant cases, after having seen how the requirements of *cic* can be and have been applied to the cases in practice. For now it is sufficient to remark that the courts and most authors regard as the gist of *cic* the disappointed trust of the plaintiff that was justified because of the special circumstances. Even though, the notion of trust or confidence is vague and cannot justify liability on its own,[257] it is together with either the special abilities or the inducing conduct of the defendant that it is correct to make him pay for damages so caused.[258]

Note finally, that *cic* concerns merely the negligent termination of negotiations. A party who wilfully causes damage to another in a manner which is *contra bonos mores* will be held liable under § 826 BGB, a rule of the law of delict or under the specific rules of the law of obligation of the German Civil Code.[259]

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[253] Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 49.

[254] Emmerich - MüKo, *supra* n. 9, Vor § 175, digit 54; v. Bar, .Vertragliche Schadensersatzpflichten ohne Vertrag? JuS 1982, 637, at 638, 639; H. Stoll, *Tatbestände und Funktionen der Haftung für culpa in contrahendo*, Festschrift für Caemmerer (1978), 435, at 452.

[255] Medicus, *Verschulden bei Vertragsverhandlungen*, in: Bundesminister der Justiz (ed.), *Gutachten und Vorschläge zur Überarbeitung des Schuldrechts*, vol. 1 (1981), at 494.; Ballerstedt, *Zur Haftung für cic bei Geschäftsabschluß durch Stellvertreter*, AcP 151 (1950/51), 501, at 505 - 506; Canaris, *Schutzgesetze - Verkehrspflichten -Schutzpflichten*; (2.) Festschrift für Larenz (1983), 27, at 105 - 107.

[256] Hopt, Nichtvertragliche Haftung außerhalb von Schadens- und Bereicherungsausgleich, *AcP 183 (1983)*,608, at 640 - 644.

[257] Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 55.

[258] D Medicus, *supra* n. 255, at 495.

[259] B.S. Markesinis, *supra* n. 247, at 69, Medicus, *supra* n. 255, at 495; M Weber, Haftung für in Aussicht gestellten Vertragsabschluß, *AcP* 192 (1992) 390, at 393.

II. Requirements

The *cic* requires (1) a specific relationship between the parties, (2) the harming conduct, (3) fault on the part of the defendant and finally (4) the causation of a damage.[260] These requirements are valid for all possible cases under *cic*. In the following, the special situation of failed negotiations will be considered within these features.

1. Relationship of the parties

Liability will only follow when the parties met in the context of some special relationship.[261] In order for legal consorting to function properly it is necessary that partners who get into contact with each other exercise mutual considerateness and diligence.[262] Not any remote connection can suffice to give rise to such duties of care. Accordingly, it has to be determined when the relations are close enough. Lawyers disagree about how to delimit the good cases. Most authors let not suffice a merely intensive social contact, but demand that the parties came together in the context of some legal transaction, which must, however, not amount to negotiations.[263] The opening of negotiations intended to lead to a contract, however, certainly creates this special relationship by virtue of law.[264] Consequently, the here examined cases, where the parties have entered into negotiations will always fulfil this requirement.

Within this requirement it is only necessary to establish that the parties are bargaining partners. At this stage of the examination one must not determine, when or if enough confidence has been inspired in order to justify the plaintiff's later reliance.

2. Harming conduct

Any case in order to give rise to an action under *cic* requires that the defendant acted in a way that harmed the plaintiff in his legitimate interests. At this stage, only the harming conduct has to be found and classified, not that it was exercised with fault.

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[260] H. Brox, *supra* n. 249, digit 56 – 58.

[261] P Gottwald, Die Haftung für culpa in contrahendo, *JuS* 1982, 877, at 877.

[262] P Gottwald, *supra* n. 261, at 877 - 878.

[263] RGZ 78, 239 (Linoleumfall): this case concerns the slightly different category of the *cic* where it wants to overcome the flaws in the German law of delictual liability. It was held that a legal relationship came into existence in preparation for a puchase - the plaintiff was a mother and her child that were knocked over in the defendant's department store by two rolls of linoleum, which have been negligently caused to fall by an assistant of the defendant. H. Brox, *supra* n. 249, digit 56; C. Canaris, *supra* n. 255, at 107 - 108.

[264] RGZ 95, 58; RGZ 120, 251; BGH 6, 333; BGH 66, 54; B. S. Markesinis, *supra* n. 247, at 64; Palandt-Heinrichs, *supra* n. 245, § 276, digit 65.

One of the situation for which liability under *culpa in contrahendo* has been acknowledged through case law, is the termination of negotiations where the defendant evoked the plaintiff's trust that the conclusion of the contract is certain.[265]

Two groups of cases can be distinguished. In each of them a different reproach is made to the defendant.

a) Misrepresentation of the ability, will or possibility to contract by conduct or omission

In the first group the defendant acts wrongful already during negotiations. He inspires trust into the conclusion of the contract, although, there is an existing or possible hindrance to the conclusion that the plaintiff doesn't know about or that is concealed to him.[266] Examples are the lack of the representative's authorisation for the negotiations[267], the need to get permission for the envisaged project[268], doubts about the feasibility of the project[269], internal difficulties[270], lacking or doubtful will to conclude the contract[271].

When the contract fails, because the flaw has been discovered in time, *cic* governs the case. The reason for the failure of the contract lies in the hindrance that the defendant knew or could have known about and didn't disclose to the plaintiff before he incurred costs.[272] This is, accordingly, not a case of actively breaking off the negotiations, but concerns the general issue which party was responsible for the failure of the contract. Therefore, it is not required that the defendant was the one who broke off the negotiations.[273]

This shows, that not merely the breaking-off of negotiations leads to liability but also any other reason that stems from the sphere of the defendant. Remembering the similar cases of *Jennings* v. *Chapman, William Lacey, Sabemo* and *Murray* v. *McLean N.O.* we see again that the reproach against the defendant is not primarily that he ended the negotiations. It is rather to condemn that he fails to reassure himself about hindrances to the contract that lie within his sphere, and

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[265] RGZ 78, 239; BGH NJW 1970, 1840; BGH JZ 1991, 199, 202; BGH 6, 333; BGH 60, 221; BGH 66, 54; BGH NJW 1975, 1774; BGH NJW 1967, 2199; WM 1972, 772; NJW 1975, 43, 44; BGH BB 1955, 429; BGH MDR 1961, 49; BGH NJW-RR 1989, 627, 628; BGH LM § 276 (Fa) Nr. 3.

[266] BGH 71, 396; BGH NJW 1975, 44; Palandt-Heinrichs, *supra* n. 245, § 276, digit 73; Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 159.

[267] BGH 6, 333; BAG NJW 1963, 1843.

[268] BGH LM (Fc) Nr. 4.

[269] BGH 71, 397.

[270] BGH NJW 1984, 867.

[271] BGH NJW 1975, 44.

[272] D Medicus, *supra* n. 255, at 495.

nevertheless, continues bargaining, thereby inspiring confidence to the plaintiff that all is in good order.[274]

b) Breaking-off negotiations without sound reason

In the second group of cases the defendant acts faultlessly during the negotiations[275], but nourishes the plaintiffs expectancy for the contract and then abandons the contract without sufficient reason.[276]

The standard of a good reason for terminating the negotiations is - in respect of the freedom not to contract - not very high. Its determination will vary in each case according to the stage and scope of the negotiations and according to which elements the defendant claimed trust for.[277] It is certainly problematic to distinguish which reasons are 'good'. Authors generally agree that not as much is expected as if a party wants to cancel a concluded contract.[278] A good reason is surely, when the performance of the contract would be a unreasonable burden in the circumstances or when the defendant would be entitled to rescission had the contract already been concluded.[279] The adjudication even let suffice that the defendant obtained a better offer or that the sales prospects for the envisaged good deteriorated. [280] But it is not permitted to take recourse to matters that are alien to the subject of the contract, e.g. to the amount of the security that the plaintiff offered for the contractual obligation.[281]

Liability requires in these cases a specifically well founded trust of the plaintiff. Otherwise, it would not be justified to hold the defendant liable, to whom nothing can be reproached during the negotiations. The simple abandoning of the bargain can only be reproached to him, when he – through particularly inducing conduct - gave rise to the plaintiff's firm belief into the prospective contract. The defendant caused such trust, for example, when he pictures the conclusion as

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[273] M. Weber, *supra* n. 259, at 394.
[274] D Medicus, *supra* n. 255, at 495.
[275] M. Weber, *supra* n. 259, at 399.
[276] BGH 71, 395; BGH NJW 1975, 1774; BGH LM (Fa) Nr. 28; Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 159; H. Choi, Die vorvertragliche Haftung (culpa in contrahendo) und der deliktsrechtliche Schutz primärer Vermögensinteressen (1991), at 199.
[277] W. Küpper, Das Scheitern von Vertragsverhandlungen als Fallgruppe der culpa in contrahendo (1989), at 241 - 248.
[278] D Medicus, *supra* n. 255, at 497.
[279] P. Gottwald, *supra* n. 261, at 879.
[280] Palandt-Heinrichs, *supra* n. 245, § 276, digit 72.
[281] BGH 76, 351; BGH LM § 276 (Fa) Nr. 11.

absolutely certain[282], when he induced the plaintiff to undertake advanced services or payments[283] or when the parties commenced their peformances[284]. The further the negotiations have advanced the more probable the liability of the defendant gets.[285]

3. Fault

Cic requires in general fault on the part of the defendant according to § 276 German Civil Code, i.e. his or his assistant's negligence. Negligence is to disregard the diligence that is necessary in traffic.[286] Such negligence consists in the first group of cases in misrepresenting the will, ability or possibility to conclude a contract without diligently examining whether the representation is true. The second group entails negligence in that the defendant breaks-off the negotiations without sound reason, i.e. by carelessly superimposing his freedom of contract onto the plaintiff despite the detrimental effects.

In some cases of an arbitrary termination of the negotiations, the judiciary took the view that one should renounce to fault. It based its attitude on an analogy to § 122 Civil Code, which obliges the party that avoids a contract to pay for the resulting damages without requiring fault.[287] Other judgements, however, insist on a faulty conduct.[288] The newest decision on this matter again renounced to the requirement, at least when only the negative interest is claimed. The bench emphasised that in a situation where the defendant arbitrarily ends the negotiations it mustn't be shown that he evoked the confidence into the conclusion of the contract with fault.[289] Indeed, the defendant's refusing of the agreement without good reason constitutes the fault in the same time. Hence, there is and should also be fault in these cases.[290] Another argument for demanding fault is that already liability under a concluded contract needs a fault of the defendant, then, precontractual liability must all the more insist on this requirement.[291]

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[282] BGH NJW 1970, 1840, BGH NJW-RR 89, 627.
[283] BGH 92, 176; BGH NJW 1961, 169; BGH LM (Fa) Nr. 3.
[284] BGH 6, 334; BGH LM (Fa) Nr. 11.
[285] Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 163.
[286] § 276 Abs. 1 German Civil Code.
[287] BGH LM § 276 (Fa) Nr. 28; BGH WM 1974, 508.
[288] BGH NJW 1975, 43; BGH NJW 1979, 915; BGH WM 1972, 772.
[289] BGH NJW-RR 1989, 627.
[290] C. Canaris, *supra* n. 255, at 91: he also requires that the plaintiff had no reasonable opportunity to safeguard his interests.
[291] H Stoll, *supra* n. 254, at 449; H. Choi, *supra* n. 276, at 206.

In all cases the defendant is bound by the trust of the plaintiff only for a reasonable period of time, otherwise the plaintiff will be liable for contributory negligence.[292]

4. Causation of the damage

The defendant must pay for the reliance damages he caused through his promising conduct.[293] The liability is limited to expenditures that were justified in the situation.[294] The plaintiff can merely recover his negative interest, hence, not the profit that he would have received under the envisaged contract, since, that would amount to obliging the defendant under the contract that he refuses to sign - freedom of contract.[295]

III. Problems of *culpa in contrahendo*

The difficulties of the *cic* do not consist in subsuming the relevant cases under this action - as it was the case for 'unjust enrichment' and 'negligent misrepresentation'. The problem is here to determine concretely which is the violated duty, where this liability is located within the system of law, and lastly, how to limit the liability reasonably.[296]

The main criticism against the doctrine is that the notions she is built on - the notions of trust and confidence - are too vague. Comparative analysis with stricter jurisdictions - as the English one - indicates, that such reasoning should only be applied for an intermediate time, until concrete policy considerations overtake and define exactly when and to which extent there is liability.[297] The fact that confidence is granted doesn't say anything about when and in how far such trust is justified and has to be legally protected. Such warnings don't necessarily intend to abolish *cic*, but aim to prevent that *cic* is used excessively as an 'all-appropriate-weapon' to grant liability based on mere subjective considerations of justice.[298] Such excessive use of *cic* is seen in its application to many very diverse cases simply because all of them display some fault / disappointment of trust happening in the precontractual phase.[299]

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[292] BGH NJW 1970 1840; Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 161.
[293] B. S. Markesinis, *supra* n. 247, at 69.
[294] BGH LM § 276 (Fc) Nr. 4; BGH WM 1976, 923; Palandt-Heinrichs, *supra* n. 245, § 276, digit 74.
[295] Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 165.
[296] P Gottwald, *supra* n. 261, at 878.
[297] K J. Hopt, *supra* n. 256, at 641.
[298] K. J. Hopt, *supra* n. 256, at 642.
[299] P. Gottwald, *supra* n. 261, at 877.

Such dangers and criticism can only be depreciated by distinguishing clear categories where *cic* applies, by determining which is their ground for liability and by laying down fixed requirement for liability in these specific categories.[300]

1. Suggestions for the basis of liability in cases of failed negotiations

We are here concerned only with the disruption of negotiations and which reasons there are for the defendant's liability in these cases.

The defendant's breaking-off of negotiations is legally reproachable, only, when the defendant exceeded his freedom of contract or vice versa violated a right of the plaintiff. How far one regards the defendant's freedom / the plaintiff's right to reach, i.e. in how far one allows the defendant to change his mind unpunished, depends on the balance of the mutual interests of the parties. As a result we must give reasons why we give more weight to the plaintiff's trust or less weight to the defendant's freedom of contract.

According to what was said before about the different opinions in respect of the ground for liability under *cic*, there is also disagreement about the basis of liability in this specific group of cases.

Some contend that the defendant **disregarded his duty to inform** the plaintiff and clarify his standing with regard to the contract.[301]

Others regard the **protection of the plaintiff's trust** as the true basis.[302] Within this group the opinion has been expressed that the defendant mustn't even have acted with fault.[303] The mere existence of confidence should be enough to forbid the defendant to break off negotiations arbitrarily.[304] As was explained above, such abandonment with lack of a good reason constitutes a fault. As a result, there is in truth no liability without fault.[305]

Lastly, some aver that the defendant has to pay damages, because he acted with fault against a binding obligation that he created by his own conduct - ***venire contra factum proprium***.[306]

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[300] P. Gottwald, *supra* n. 261, at 878.
[301] BAG NJW 1963, 1843.
[302] H Brox, *supra* n. 249, digit 56; Palandt-Heinrichs, *supra* n. 245, § 276, digit 72.
[303] See above the remarks to an analogy to § 122 Civil Code under 'fault'.
[304] K. Larenz, *supra* n. 4, at 416.
[305] P Gottwald, *supra* n. 261, at 879.
[306] Staudinger, *supra* n. 248, prelim. remark to §§ 275 ff., digit 66; Emmerich - MüKo, *supra* n. 9, Vor § 275, digit 161.

2. The right path

As has been suggested earlier, the gist of defendant's liability is the unjustified disappointment of the plaintiff's trust which was in turn justified by the defendant's conduct. One cannot find a convincing explanation for liability by looking at only one of the parties, either the plaintiff's trust or the defendant's duty. Both positions are mutually dependant.

On the one side, the mere confidence of the plaintiff into the defendant's endeavour to bring about a contract wouldn't be sufficient reason for liability, also mere strangers can trust. The plaintiff must reasonably trust. One could contend that already the beginning of negotiations is legally relevant and brings about justified trust into the defendant's care and diligence as can be expected in all legal transactions.[307] Such an assumption would, however, completely undermine the freedom of contract. The mere beginning to negotiate doesn't justify to confidently anticipate a contract if there are no further indicators - at least the continuous progress of the negotiations[308] - that a contract will certainly come about. Therefore, the defendant's conduct or ability in the case must be considered. The conduct of the defendant must imply that he undertook to exercise diligence and care towards his negotiating partner.[309] Furthermore, there is no reason to hold him liable if he fulfils his undertaking. Thus, he must - according to the two groups of cases presented above - either have omitted to verify if he has the ability and will to contract, or he must have broken off the negotiations without a weighty reason.[310]

On the other side, the defendant is merely bound because of the plaintiff's trust and reliance. His conduct alone would not justify liability since he couldn't harm anyone with it. A reasonable plaintiff incurs expenses only after and when trusting into the defendant's behaviour with regard to the envisaged contract.[311] Also, the law allows one-sided declarations to be bound only in exceptional cases. Since precontractual dealings are typically two-sided and contain mutual expectancies, such an exception is here not justified.[312] As a result, liability requires elements from

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[307] P Gottwald, *supra* n. 261, at 879.
[308] K. Ballerstedt, *supra* n. 255, at 504, 506.
[309] P Gottwald, *supra* n. 261, at 879, as will mostly be the case when a professional person acts in his professional capacity: K. Ballerstedt, *supra* n. 255, at 521.
[310] It certainly help, when determining right at the beginning exactly which trust the defendant inspired: that he has the ability, will and possibility to contract or that he will surely contract.
[311] K. Ballerstedt, *supra* n. 255, at 506.
[312] P Gottwald, *supra* n. 261, at 879.

the two spheres of plaintiff and defendant: conduct on the one side, resulting trust on the other side.

Accordingly, of the three above-mentioned suggestions, the latter two together build the basis of liability for breaking off negotiations. They are both originating from the principle of good faith, which protects justified faith on the plaintiff's side and forbids contradictory behaviour on the defendant's side.

The first proposition - the defendant violated his duty to correctly inform the plaintiff - does not truly explain the reason for liability: why is there a duty to inform the plaintiff about relevant facts, even though the parties act in the precontractual , i.e. not *per se* binding sphere? The duty to inform the plaintiff can only arise from entering into some legally relevant relationship. The precontractual relationship becomes legally relevant only when the parties achieved a certain closeness where they justifiably rely on each other, thus, back to conduct and legitimate confidence.[313]

It is submitted, consequential to the finding of liability's basis, that a three-step examination must take place: (1) conduct of the defendant which makes a reasonable person trust into his will and ability to contract, (2) as a result trust and reliance of the plaintiff and (3) disappointment of that trust through (a) faultily representing will and ability during the negotiations or (b) disrupting negotiations for no sound reason.

IV. Conclusion

The *cic*, although, criticised for being too broad and vague a doctrine, applies to cases of failed negotiations. The causing of the failure of negotiations is a fixed category within *cic*, recognised and refined by case law.[314] The requirements for liability are laid down, but are partly imponderable. For example, when is the conduct such, that a reasonable person would trust and rely on it? When is a reason good enough to justify the ending of the negotiations? This imponderableness, however, doesn't justify to deny a claim. Mostly, it will be obvious whether the plaintiff was entitled to believe into the future contract, e.g. because of written assurances, requests to start performing etc. In case of doubt one will hold that in view of the principle of freedom of contract the plaintiff doesn't recover - he can only trust legitimately, when a reasonable

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[313] K. Ballerstedt, *supra* n. 255, at 506.
[314] C. Canaris, *supra* n. 255, at 106.

person in his place would also be sure that a contract will be concluded, otherwise he is a risk-taker.[315]

Legitimate confidence is a recognised value in German law and would forbid to deny protection to a plaintiff who could reasonably rely on his vis-à-vis. The mutual trust during negotiations is worth of protection, because the parties entered into a special bond. As opposed to mere strangers the parties to negotiations open their legal sphere to each other.[316] Other approaches than the legitimate and disappointed trust don't offer more security and less substance - e.g. self-binding without a contract (from which implications can one infer self-binding?) or delictual professional liability (are duties to take care limited to a professional capacity, why and how far?).[317] All of them go back to legitimate confidence.

An action under *culpa in contrahendo* offers apt tools to argue whether and to what extent the plaintiff should be able to retrieve his expenses.

E. Final considerations

The previous chapters have shown how national legal systems mainly deal with the unjustified abandonment of negotiations. Finally, it should be noted that these were merely the main grounds for liability, but not exclusive ones.

I. Other basis of liability

Common law systems have made several very different inroads into the freedom not to contract. In England it was mainly dealt with precontractual liability under unjustified enrichment. But there was also a case where negligent misrepresentation was the basis of liability.[318]

Another interesting concept that was applied is the doctrine of promissory estoppel. In the American case of *Hoffman* v. *Red Owl Stores* the plaintiff had incurred outlay at the defendant's request, who in turn had represented that there was a safe expectation of a franchise contract. The plaintiff received compensation under the promissory estoppel, since the defendant acted contradictory to his previous promise, that was held to bind him insofar.[319] Australian law has

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[315] W. Küpper, *supra* n. 277, at 146 - 147.
[316] W. Küpper, *supra* n. 277, at 40 - 41, 146.
[317] C. Canaris, *supra* n. 255, at 106.
[318] *Box* v. *Midland Bank* (1979) 2 Lloyds Rep. 391.
[319] 133 NW 2d 267.

shared the view of using promissory estoppel as ground of relief.[320] Only English law barred the way to this remedy. It maintains that promissory estoppel serves merely as a shield and not as a sword, i.e. one can only use estoppel as a defence for claims of the defendant, but not as a basis for claiming compensation.[321] The older English cases like e.g. *Brewer Street* would be less difficult to explain on the basis of estoppel. In these judgements the House of Lords had to make complicated and unconvincing assumptions about the binding force of the defendants' previous contractual undertaking to bear the costs, although, the condition for that undertaking - a final contract - didn't come about. New voices consider if promissory estoppel might give a cause of action. The premise is that estoppel in its original application prevents the defendant from enforcing a right, when it is inequitable to do so, that is, when the plaintiff relied on a representation of the defendant that he will not enforce that right. Why then not extending estoppel to a more positive expectation, i.e. that the plaintiff can gain a right, if the defendant so represented his position?[322] Another

common law approach is purely contractual. One could find, that the defendant had already entered into a conditioned contract. When he refuses to fulfil the contract for another reason than the failure of the condition, he is contractually bound to pay for damages caused by such violation of the contract.[323] This solution is not viable, as we have seen for example in *Sabemo, Regalian* and *Murray* v. *McLean*, when the parties expressly fixed their status to a precontractual one and when the condition is the conclusion of the contract itself.

A still different approach is to be found in French law which bases its liability for failed negotiations on the law of delict and achieves results that are very similar to the German *cic*.[324] It is based on the fact that the plaintiff (1) suffered a certain damage (dommage),[325] that the defendant committed a precontractual fault, which consists in not negotiating loyally and with good faith as a reasonable person would do[326] and (3) that there is a causal link between the

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[320] *Waltons Stores (Interstate) Ltd.* v. *Maher* (1988) 164 CLR 387.

[321] C Davis, Estoppel: An Adequate Substitute for Part Performance? *OJLS* 13 (1993) 99, at 117; M. P. Thompson, From Representation to expectation: Estoppel as a Cause of Action, *CLJ* 42 (1983) 257, at 266; B. S. Markesinis, *supra* n. 247, at 70.

[322] M. P. Thompson, *supra* n. 321, at 267 - 268, for acquiring land or an interest on land, estoppel has already produced rights in the form of propietary estoppel.

[323] M. Weber, *supra* n. 259, at 406.

[324] B. S. Markesinis, *supra* n. 247, at 64.

[325] J. Schmidt-Szalewski, La Période Précontractuelle en Droit Francais, RIDC 42 (2-1990) 545, at 548 – 550.

[326] J. Schmidt-Szalewski, *supra* n. 325, at 550.

damage and the fault[327]. As in German law, it is submitted, that the plaintiff could reasonably trust into the conclusion of the contract, and consequently, the defendant cannot disrupt the negotiations unpunished.

II. Reasonable extent of liability

Under each of the actions the plaintiff recovers his expenses either as damage or as *quantum meruit*.[328] It is justified to grant the plaintiff such expenses as far as he wouldn't have to bear them anyway e.g. as tendering costs and didn't contribute to their extent. Apart from the restitutionary claim all suggested remedies give room to consider the plaintiff's contributing to the damage.

Lost profits of the anticipated contract should, however, be excluded from liability. Such lost profits are typically contractual damages as they give the plaintiff the benefit of the bargain that was not reached.[329] Consequently, the defendant would have to pay the same amount as if he would have concluded the contract, thus, as if he was obliged to enter into the contract without receiving his share of the deal himself. Such an extent of his liability is in view of the freedom of contract not justifiable. Only, when the parties agreed to a binding obligation can they recover expectation losses, before that stage there is mere reliance loss.

Business that the plaintiff has foregone during the negotiations constitutes in principle a reliance loss. He refuses other gaining opportunities, because he rightly trusts that the work he is doing at the moment will lead to a contract, and is, therefore, a priority. The plaintiff should, however, show which business he has foregone and to which sums these lost profits amount. He cannot claim a mere estimated lump-sum, but must justify his demand by the high probability that he would have gained X amount.[330]

F. Conclusion

It has been established that there is liability for causing negotiations to fail despite the freedom not to contract. The reason for liability is the creation of legitimate trust between the parties which the defendant culpably disappoints when disrupting the negotiations. The defendant shows that he

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[327] J. Schmidt-Szalewski, *supra* n. 325, at 553.

[328] The *quantum meruit* will generally be measured according to the costs incurred, although, the claim could in principle be assessed by the court with the aid of the objective value of the services. Then the plaintiff wouldn't recover his or his sub-contractor's profit margin for these services.

[329] E. A. Farnsworth, *supra* n. 4, at 223.

[330] Palandt-Heinrichs, *supra* n. 245, § 252, digit 1.

renounces - at least partly - to his freedom not to contract by showing a sincere interest into the conclusion of the envisaged contract.[331]

Countries that recognise the legal institute of *culpa in contrahendo* do, indeed, still grapple with the extent of liability and the legal justification of such liability. But the reasons for liability have been more or less disclosed and the case law has established fixed requirements that suit these situations. The German law also showed, that two groups of cases can be distinguished: one where the defendant misrepresents during the negotiations, and another, where he acts correctly during the bargaining process, but abandons the agreement with fault.

Negligent misrepresentation is appropriate when a misrepresentation can be discerned. When correctly examining the defendant's conduct one must admit, that there is no *mis*representation when the defendant's rightly shows his state of mind and only later changes his stand.

The English law of restitution seems least appropriate to deal with the arbitrary termination of negotiations. It depends on the benefit of the defendant which is in many cases extremely difficult to argue. Recourse to doctrines concerning the subjective devaluation is necessary such as the principle of free acceptance, which in the same time creates a ground for restitution, establishes the defendant's benefit and bars the defence of change of position. Such doctrines are surely as daring as one based on good faith, promissory estoppel or unjust sacrifice and helps less, as it blurs and complicates the already difficult issue, why there should or should not be liability.

Signed by candidate

[331] M. Weber, *supra* n. 259, at 401, W. H. Holmes, *supra* n. 102, at 796.